FR TYK COMPILATION

This compilation covers all TYK question from FR study material so, if you have practiced qns from study material then you can carry this compilation in exam instead of carrying the 4 module of study material. It will be more convenient.

Page Number

Sr.	Chapter Name	Pg No.
1	Chapter 2: Conceptual Framework for Financial Reporting under Indian Accounting Standards (Ind AS)	16
2	Unit 1: Ind AS 1 “Presentation of Financial Statements”	18
3	Unit 2: Ind AS 34 “Interim Financial Reporting”	27
4	Unit 3: Ind AS 7 “Statement of Cash Flows”	33
5	Unit 1: Ind AS 8 “Accounting Policies, Changes in Accounting Estimates and Errors ”	47
6	Unit 2: Ind AS 10 “Events after the Reporting Period”	57
7	Unit 3: Ind AS 113 “Fair Value Measurement”	63
8	Chapter 5: Ind AS 115 “Revenue from Contracts with Customers”	73
9	Unit 1: Ind AS 2 “Inventories”	82
10	Unit 2: Ind AS 16 “Property, Plant and Equipment”	89
11	Unit 3: Ind AS 23 “Borrowing Costs”	103
12	Unit 4: Ind AS 36 “Impairment of Assets”	114
13	Unit 5: Ind AS 38 “Intangible Assets”	132
14	Unit 6: Ind AS 40 “Investment Property”	141
15	Unit 7: Ind AS 105 “Non-current Assets Held for Sale and Discontinued Operations”	149
16	Unit 8: Ind AS 116 “Leases”	159
17	Unit 1: Ind AS 41 “Agriculture”	166
18	Unit 2: Ind AS 20 “Accounting for Government Grants and Disclosure of Government Assistance”	174
19	Unit 3: Ind AS 102 “Share Based Payment”	183
20	Unit 1: Ind AS 19 “Employee Benefits”	197
21	Unit 2: Ind AS 37 “Provisions, Contingent Liabilities and Contingent Assets”	205
22	Unit 1: Ind AS 12 “Income Taxes”	210
23	Unit 2: Ind AS 21 “The Effects of Changes in Foreign Exchange Rates”	221
24	Unit 1: Ind AS 24 “Related Party Disclosures”	231
25	Unit 2: Ind AS 33 “Earnings per Share”	238
26	Unit 3: Ind AS 108 “Operating Segments”	246
27	Chapter 11: Accounting and Reporting of Financial Instruments Ind AS 109	252
28	Chapter 12: Ind AS 103 “Business Combinations”	268
29	Chapter 13: Consolidated and Separate Financial Statements of Group Entities Ind AS 27., 28, 110 & 111	299
30	Chapter 14: Ind AS 101 “First-time Adoption of Indian Accounting Standards”	335
31	Chapter 15: Analysis of Financial Statements	343
32	Chapter 16: Professional and Ethical Duty of a Chartered Accountant	386
33	Chapter 17: Accounting and Technology	389

Ind AS	Question - Initial Wording	Topic	Pg No
ACCOUNTING & TECHNOLOGY TYK-1	What are the steps involved to automate the process to determine whether it is appropriate to aggregate Segments 1 and 2 with reference to Ind AS 108 'Operating Segments'?		17.33
ACCOUNTING & TECHNOLOGY TYK-2	Advice the steps to automate the process to perform the above tasks on behalf of New Way Ltd		17.44
ACCOUNTING & TECHNOLOGY TYK-2	Define criteria for identifying contracts with customers, such as enforceable rights and obligations, agreement terms, and consideration.		17.44
ACCOUNTING & TECHNOLOGY TYK-2	Establish rules to link relevant transactions to specific contracts and assign unique identifiers to each contract		17.44
ACCOUNTING AND TECHNOLOGY TYK			
Analysis of F Stt CS-1	Analyze whether the above accounting treatment made by the accountant is in compliance with the relevant Ind AS. If not, advise the correct treatment of housing loan, interest and other expenses	Ind AS 109+19 issue	15.11
Analysis of F Stt CS-1	You are required to explain how the housing loan should be reflected in the Ind AS	Ind AS 109+19 issue	15.11
Analysis of F Stt CS-2	Analyse whether the above accounting treatment made by the accountant is in compliance with the Ind AS. If not, advise the correct treatment alongwith the necessary workings	Ind AS 105 issue	15.14
Analysis of F Stt CS-3	Analyse whether the above accounting treatment made by the accountant in regard to financial year ending on 31.0.20X2 is in compliance of the Ind AS	Ind AS 2+10 issue	15.16
Analysis of F Stt CS-4	Analyse whether the view adopted by the CFO of Sun Ltd is in compliance of the Ind AS. If not, advise	Ind AS 36 issue	15.18
Analysis of F Stt CS-5	You are required to ascertain that whether the financial statements of Softbharti Pvt. Ltd. are correctly presented	Ind AS and Division II to Schedule III of the Companies Act, 2013	15.19
Analysis of F Stt CS-6a	Advice on the treatment of borrowing costs in its financial statements for the year ending 31 March 20X2.	Ind AS 23 issue	15.25
Analysis of F Stt CS-6b	Advice on the treatment of the acquisition, extension, review and sale of players' registrations	Ind AS 38+36 issue	15.25
Analysis of F Stt CS-6c	How to take account of the naming rights in the valuations of the stadium and the potential implications of the financial regulations imposed by the legislations	Ind AS 113 issue	15.26
Analysis of F Stt CS-7a	Advice on the treatment of the agreement with Seemanchal as well as the accounting for the irrecoverable gas	Ind AS 111+16 issue	15.29
Analysis of F Stt CS-7b	Neelanchal wants to account for the contract with Uttaranchal in accordance with Ind AS 109 Financial Instruments and seeks your inputs in this regard	Ind AS 109 issue	15.29
Analysis of F Stt TYK			
Analysis of F Stt TYK-1	Analyse whether the accounting policies adopted by the Venus Ltd. in relation to these properties is in accordance with Ind AS. If not, advise the correct treatment alongwith working for the same		15.33
Analysis of F Stt TYK-2	Analyse whether the above accounting treatment made by the accountant is in compliance of the Ind AS. If not, advise the correct treatment along with working for the same		15.34
Analysis of F Stt TYK-3	Analyse whether the above accounting treatment made by the accountant is in compliance of the Ind AS. If not, advise the correct treatment along with working for the same		15.34
Analysis of F Stt TYK-4	Analyse whether the above accounting treatment made by the accountant is in compliance of the Ind AS. If not, advise the correct treatment along with working for the same		15.34

Analysis of F Stt TYK-5	Being Finance & Accounts manager, you are required to identify the errors and misstatements if any in the balance sheet of Master Creator Private Limited and prepare corrected balance sheet with details on the face of the balance sheet i.e. no need to prepare notes to accounts, after considering the additional information. Provide necessary explanations/workings for the treated items, wherever necessary		**15.37**
Analysis of F Stt TYK-6	Prepare Ind AS Impact Analysis Report (Extract) for HIM Limited for presentation to the management wherein you are required to discuss the corresponding differences between Earlier IGAAP (AS) and Ind AS against each identified issue for preparation of transition date balance sheet. Also pass journal entry for each issue		**15.38**
Conceptual framework TYK			
Conceptual framework TYK-1	Prepare notes for the directors of Jayant Ltd. to discuss the issue raised in the shareholders' email with reference to the Conceptual Framework wherever appropriate.		**2.70**
IND AS 1 TYK			
IND AS 1 TYK-1	Assuming that the production time was say 15 months and the time lag between the date of sale and collection from customers is 13 months, will the answer be different?	Current or non-current - Trade rec & Inventory - Prod time > 12m	**3.68**
IND AS 1 TYK-1	Will the inventory and the trade receivables be current in nature?	Current or non-current - Trade rec & Inventory - Prod time < 12m	**3.68**
IND AS 1 TYK-2	As on 31st March, 20X2, how should the entity classify the loan?	Current or non-current - loan payable on demand	**3.68**
IND AS 1 TYK-2	**Assume that in anticipation that it may not be able to get the promoter's contribution by due date, in February 20X2, the entity approached the bank and got the compliance date extended upto 30th June, 20X2 for getting promoter's contribution. In this case will the loan classification as on 31st March, 20X2 be different from (a) above?**	**Current or non-current - breach of loan covenant**	**3.68**
IND AS 1 TYK-3	Advise on the classification of the liability as current / non-current.	Current or non-current - breach of material provision of long-term loan arrangement	**3.69**
IND AS 1 TYK-4	Identify and present the transactions in the financial statements as per Ind AS 1	Presentation of items in P/L & OCI	**3.69**
IND AS 1 TYK-5	**Evaluate the above matters with respect to preparation and presentation of a general-purpose financial statement.**	**Presentation of items**	**3.70**
IND AS 1 TYK-6	**Can management present the third statement of profit and loss as an additional comparative in the general-purpose financial statements?**	**third statement of profit and loss**	**3.70**
IND AS 1 TYK-6	**Can management present third statement of profit and loss only as additional comparative in the general-purpose financial statements without furnishing other components (like balance sheet, statement of cash flows, statement of change in equity) of financial statements?**	**third statement of profit and loss**	**3.70**
IND AS 1 TYK-6	**If management present third statement of profit and loss in the general-purpose financial statement as comparative, is it necessary that this statement should- be compliant of Ind AS?**	**third statement of profit and loss**	**3.70**
IND AS 1 TYK-7	Is it necessary to provide the third balance sheet at the beginning of the preceding period in this case?	Third balance sheet	**3.71**
IND AS 1 TYK-7	The company wants to correct the errors during financial year 20X2-20X3 by giving impact in the figures of current year only. Is the contention of the management, correct?	Third balance sheet - Correction of errors	**3.71**
IND AS 1 TYK-8	Can the security deposit of 2 crore taken by the company from contractors be presented as non-current?	Cuurent or non current - Security Deposit	**3.72**

IND AS 1 TYK-8	Can the security deposit of 5 crore made by the company with the customers be presented as current?	Cuurent or non current - Security Deposit	**3.72**
IND AS 1 TYK-8	The company wants to present the trade payables as non-current despite the fact that these are due within the operating cycle of the company. Does the decision of presenting the same as non-current is correct?	Cuurent or non current - Trade rec - 15m time	**3.72**
IND AS 1 TYK-8	The company wants to present the trade receivable as current despite the fact that these are receivables in 15 months' time. Does the decision of presenting the same as current is correct?	Cuurent or non current - Trade rec - 15m time	**3.72**
IND AS 1 TYK-9	**Expenses incurred by a holding company on behalf of subsidiary, which is reimbursed by the subsidiary - whether in the separate books of the holding company, the expenditure and related reimbursement of expenses can be offset?**	**Offsetting - Exp on behalf of Subsi**	**3.72**
IND AS 1 TYK-9	Is offsetting permitted under the following circumstances?	Offsetting	**3.72**
IND AS 1 TYK-9	**When services are rendered in a transaction with an entity and services are received from the same entity in two different arrangements, can the receivable and payable be offset?**	**Offsetting - Same entity - 2 arrangement - Rec & Pay**	**3.72**
IND AS 1 TYK-9	**Whether profit on sale of an asset against loss on sale of another asset can be offset?**	**Offsetting - Pft on sale and loss on other**	**3.72**
Ind AS 10 TYK			
Ind AS 10 TYK-1	Whether the management view is correct in accordance with the guidance given in Ind AS 10?		**4.80**
Ind AS 10 TYK-2	Comment on the company's views in the light of Ind AS 10		**4.80**
Ind AS 10 TYK-3	Comment on the company's views		**4.81**
Ind AS 10 TYK-4	How will you treat the above in the financial statements for the year ended 31st March, 20X2		**4.81**
Ind AS 10 TYK-5	whether A Ltd. is required to remeasure its provision and what would be the accounting treatment of the cost that will be recovered by A Ltd., which has already been charged to the Statement of Profit and Loss as an expense for the year 20X1-20X2?		**4.81**
Ind AS 10 TYK-6	Whether duty drawback credit should be treated as an adjusting event?		**4.81**
Ind AS 10 TYK-7	State whether discount will be adjusted from the sales at the end of the reporting period		**4.82**
Ind AS 10 TYK-8	Whether the fraud related to 20X1-20X2 discovered after the end of the reporting period but before the date of approval of financial statements for 20X3-20X4 is an adjusting event?		**4.82**
Ind AS 10 TYK-9	Whether these events are adjusting or non-adjusting events and explain the treatment accordingly.		**4.82**
Ind AS 101 TYK			
Ind AS 101 TYK-1	If business combinations are restated, whether certain other exemptions, such as the deemed cost exemption for property, plant and equipment (PPE), can be adopted?		**14.47**
Ind AS 101 TYK-2	Whether use of fair values as deemed cost on the date of transition and use of revaluation model in the first annual Ind AS financial statements would amount to a change in accounting policy?		**14.47**
Ind AS 101 TYK-3	Whether the Company is permitted to do so?	Para 46/46A of AS 11	**14.47**
Ind AS 101 TYK-4	How would the company be required to adjust the foreign exchange fluctuation already capitalised to the cost of property, plant and equipment under previous GAAP?		**14.48**
Ind AS 101 TYK-5	Suggest the accounting adjustments which are required to be made in the opening Balance Sheet as on 1st April, 20X1		**14.49**

Ind AS 101 TYK-6	What is the balance of total equity (Equity and other equity) as on 1st April, 20X1 after transition to Ind AS? Show reconciliation between total equity as per AS (Accounting Standards) and as per Ind AS to be presented in the opening balance sheet as on 1st April, 20X1		**14.50**
Ind AS 101 TYK-7	State whether the accounting treatment of the grants in the nature of promoters' contribution as per AS 12 is also permitted under Ind AS 20 Accounting for Government Grants and Disclosure of Government Assistance. If not, then what will be the accounting treatment of such grants recognised in capital reserve as per previous GAAP on the date of transition to Ind AS		**14.50**
Ind AS 102 TYK			
Ind AS 102 TYK-1	Calculate the expense for years 1 & 2?		**7.110**
Ind AS 102 TYK-10	What would be the accounting treatment in the books of Company P and Company S?		**7.113**
Ind AS 102 TYK-11	How much expense and liability is to be recognized at the end of each year? Pass the Journal entries		**7.113**
Ind AS 102 TYK-2	Calculate the expense for years 1 and 2		**7.110**
Ind AS 102 TYK-3	Pass the journal entry in the books of company P & company B?		**7.110**
Ind AS 102 TYK-4	Define expenses related to such share-based payment plan in each year subject to the below scenarios-		**7.111**
Ind AS 102 TYK-5	Calculate the expenses for next 3 years in respect of share-based payment?		**7.111**
Ind AS 102 TYK-6	Pass the journal entries		**7.111**
Ind AS 102 TYK-7	Pass the journal entries		**7.112**
Ind AS 102 TYK-8	What would be the difference if at the end of the second year of service (i.e. at 31st March 20X3), P Ltd. modifies the terms of the award to require only three years of service?		**7.112**
Ind AS 102 TYK-9	Suggest the suitable accounting treatment for these transaction as on 31 st March, 20X3		**7.113**
Ind AS 103 TYK			
Ind AS 103 TYK-1	**Determine the accounting under acquisition method for the business combination by Company A**		**12.121**
Ind AS 103 TYK-10	How should contingent consideration payable in relation to a business combination be accounted for on initial recognition and at the subsequent measurement as per Ind AS in the following cases		**12.124**
Ind AS 103 TYK-11	Suggest the accounting treatment of the above transaction under applicable Ind AS		**12.125**
Ind AS 103 TYK-12	You are required to provide your detailed responses to the following, along with reasoning and computation notes		**12.128**
Ind AS 103 TYK-12a	What should be the goodwill or bargain purchase gain to be recognised by H Ltd. in its financial statements for the year ended 31st March, 20X7. For this purpose, measure non-controlling interest using proportionate share of the fair value of the identifiable net assets of S Ltd		**12.128**
Ind AS 103 TYK-12b	Will the amount of non-controlling interest, goodwill, or bargain purchase gain so recognised in (a) above change subsequent to 31st March, 20X7? If yes, provide relevant journal entries		**12.128**
Ind AS 103 TYK-12c	What should be the accounting treatment of the contingent consideration as on 31st March, 20X7?		**12.128**
Ind AS 103 TYK-13	You need to determine the following		**12.130**
Ind AS 103 TYK-13-1	Whether the above acquisition falls under business or asset acquisition as defined under business combination standard Ind AS 103?		**12.130**
Ind AS 103 TYK-13-2	Determine the acquisition date in the above transaction?		**12.130**
Ind AS 103 TYK-13-3	Prepare Journal entries for the above-mentioned transaction?		**12.130**

Ind AS 103 TYK-13-4	Draft the Balance Sheet for Company X based on your analysis in Part 1 above as at acquisition date		**12.130**
Ind AS 103 TYK-14	Calculate the share-based payment values?		**12.131**
Ind AS 103 TYK-2	Calculate the fair value of the consideration transferred measure goodwill and prepare consolidated balance sheet as on 31st December, 20X1		**12.122**
Ind AS 103 TYK-3	Comment on the treatment done by Bank F		**12.122**
Ind AS 103 TYK-4	Find the value at which NCI has to be shown in the financial statements		**12.122**
Ind AS 103 TYK-5	Comment on the treatment to be done based on the facts given in the question		**12.122**
Ind AS 103 TYK-6	State whether the procedures followed by A and the resulting measurements are appropriate or not. Also calculate the bargain purchase gain in the process		**12.122**
Ind AS 103 TYK-7	Is the combination of entities A and B a combination of entities under common control?		**12.123**
Ind AS 103 TYK-8	Calculate the gain or loss on acquisition of Beta Pvt. Ltd. and also show the journal entries for accounting of its acquisition. Also calculate the value of the non-controlling interest in Beta Pvt. Ltd. on the basis of proportionate interest method, if alternatively applied?		**12.123**
Ind AS 103 TYK-9	Compute the impairment of goodwill in the consolidated financial statements of ABC Ltd. under both the methods permitted by Ind AS 103 for the initial computation of the non- controlling interest in JKL Ltd. at the acquisition date		**12.124**
Ind AS 105 TYK			
Ind AS 105 TYK-1	Comment whether the property can be classified as held for sale at the reporting date i.e. 31st March, 20X1		**6.352**
Ind AS 105 TYK-2	Recommend whether the factory should be shown as held for sale as on 31st March, 20X1		**6.352**
Ind AS 105 TYK-3-1	Assess whether the manufacturing unit can be classified as held for sale and reasons there for. If yes, then at which date?		**6.353**
Ind AS 105 TYK-3-2	Measure the manufacturing unit on the date of classification as held for sale		**6.353**
Ind AS 105 TYK-3-3	Measure the manufacturing unit at the end of the year		**6.353**
Ind AS 105 TYK-4	Compute the value of all assets/ labilities within the disposal group as on the following dates in accordance with Ind AS 105		**6.355**
Ind AS 105 TYK-5	Suggest how the proposed sale of the division will be reported in the interim financial statements for the quarter ended 30th June, 20X1 giving relevant explanations		**6.356**
Ind AS 105 TYK-6	Identify which of the following is a disposal group at 31st March 20X1		**6.356**
Ind AS 108 TYK			
Ind AS 108 TYK-1	Which of the segments would be reportable under the criteria identified in Ind AS 108?		**10.129**
Ind AS 108 TYK-2	Based on the above information, comment how X Ltd. would disclose information about reportable segment revenue, profit or loss, assets and liabilities for financial year 20X1-20X2		**10.130**
Ind AS 108 TYK-3	State the cost formula to be used for Ind AS 108 disclosure purposes		**10.130**
Ind AS 108 TYK-4	Based on the quantitative thresholds, state which of the above segments A to E would be considered as reportable segments for the year ending 31st March, 20X1		**10.131**
Ind AS 109 TYK			
Ind AS 109 TYK-1	Compute the value of loan initially to be recognised and amortised cost for all subsequent years		**11.223**
Ind AS 109 TYK-1	You are required to record the entries for the year ended 31 December 20X1, for the transaction		**11.223**
Ind AS 109 TYK-2	Record journal entries in the books of Wheel Co. Limited considering the requirements of Ind AS 109		**11.225**

Ind AS 109 TYK-3	Record journal entries in the books of Wheel Co. Limited till 31 December 20X3, after giving effect of the changes in the terms of the loan on 31 December 20X2		**11.225**
Ind AS 109 TYK-4	You are required to separate the debt and equity components at the time of issue and show the accounting entries in Company's books at initial recognition.		**11.225**
Ind AS 109 TYK-5	Explain how will the Company account for the above loan notes in the financial statements for the year ended 31 March 20X2?		**11.226**
Ind AS 109 TYK-6	Provide the accounting treatment of financial guarantee as per Ind AS 109 in the books of Sun Ltd., on initial recognition and in subsequent periods till 31 March 20X3		**11.226**
Ind AS 110 TYK			
Ind AS 110 TYK-1	Determine how should X Limited account for its investment in Y Limited in its consolidated financial statements after the issue of convertible preference shares by Y Limited to Z Limited?		**13.197**
Ind AS 110 TYK-10	Prepare consolidated Balance Sheet after disposal as at 31st March, 20X2 when Reliance Ltd. group sold 90% shares of Reliance Jio Infocomm Ltd. to independent party for 1000 thousand		**13.204**
Ind AS 110 TYK-11	Pass necessary accounting entries in individual and consolidation situations		**13.204**
Ind AS 110 TYK-12	What would be the accounting treatment on loss of control in the consolidated financial statements of AB Limited?		**13.205**
Ind AS 110 TYK-13	Calculate the closing balance of Investor Ltd.'s investment in XYZ Ltd. as at 31st March, 2020 as per the relevant Ind AS		**13.205**
Ind AS 110 TYK-14	Suggest the suitable accounting treatment of the above transaction as per applicable Ind AS		**13.206**
Ind AS 110 TYK-15	Secondly, if all other facts remain the same as above except that G Limited and D Limited are both owned by an Individual (say, Mr. X) instead of Gamma Limited, then explain whether GD Limited can avail the exemption from the preparation and presentation of consolidated financial statements		**13.206**
Ind AS 110 TYK-2	Calculate how the investment in O Limited will be accounted in the consolidated financial statements of M Limited?		**13.197**
Ind AS 110 TYK-3	Determine how AB Limited should account for such reduction in interest in the associate?		**13.197**
Ind AS 110 TYK-4	Prepare consolidated Balance Sheet as at March 31, 20X2		**13.198**
Ind AS 110 TYK-5	Prepare consolidated Balance Sheet as at March 31, 20X2		**13.200**
Ind AS 110 TYK-6	Prepare the Consolidated Balance Sheet as at March 31, 20X2 of group of entities Blue Heavens Ltd. and Orange County Ltd.		**13.201**
Ind AS 110 TYK-9	Prepare consolidated Balance Sheet after disposal as at 31st March, 20X2 when P Pvt. Ltd. group sold 100% shares of S Pvt. Ltd. to independent party for 3,000 millions		**13.203**
Ind AS 113 TYK			
Ind AS 113 TYK-1	The fair value of the asset, if market A is the principal market, and		**4.117**
Ind AS 113 TYK-1	The fair value of the asset, if none of the markets is principal market		**4.117**
Ind AS 113 TYK-2	Determine the highest and best use of the land		**4.118**
Ind AS 113 TYK-3	What will be the fair value of ABC Ltd.'s investment in XYZ Ltd. as on the balance sheet date?		**4.118**
Ind AS 113 TYK-4	Determine value per share of PT Ltd. as per Income Approach		**4.118**
Ind AS 113 TYK-5	Determine the Equity value of KK Ltd. as on the measurement date on the basis of above details		**4.119**
Ind AS 113 TYK-6(i)	On what basis will the land be fair valued under Ind AS?		**4.119**
Ind AS 113 TYK-6(ii)	What will be your answer if the quoted price of similar companies were available and can be used for fair valuation of the shares?		**4.119**

Ind AS 113 TYK-7	You are required to calculate the fair value of the asset retirement obligation		**4.120**
Ind AS 113 TYK-8	Determine the fair value of Entity A's investment in XYZ's shares.		**4.121**
Ind AS 115 TYK			
Ind AS 115 TYK-1	How revenue for these non-monetary transactions in the area of advertising will be recognized and measured?		**5.146**
Ind AS 115 TYK-10	Determine the transaction price.		**5.149**
Ind AS 115 TYK-11	Determine the nature of license.		**5.149**
Ind AS 115 TYK-2	How should revenue be measured in this case?		**5.146**
Ind AS 115 TYK-3	Whether Company X should include cost of the air conditioners in measure of its progress of performance obligation? How should revenue be recognized for the year ended March 20X1?		**5.147**
Ind AS 115 TYK-4	When should G Ltd. recognize revenue from sale of machinery to P Ltd. in accordance with Ind AS 115?		**5.147**
Ind AS 115 TYK-5	What is the transaction price in this arrangement?		**5.147**
Ind AS 115 TYK-6	How should entity J determine the transaction price?		**5.148**
Ind AS 115 TYK-7	How should entity K determine the transaction price?		**5.148**
Ind AS 115 TYK-8	How should the manufacturer determine the transaction price?		**5.148**
Ind AS 115 TYK-9	Determine the transaction price.		**5.149**
Ind AS 116 TYK			
Ind AS 116 TYK-1	**Whether the lessor has substantive substitutions rights and whether the arrangement contains a lease?**		**6.514**
Ind AS 116 TYK-2	**Whether it can be established that M is having the right to control the use of identified asset?**		**6.514**
Ind AS 116 TYK-3	**Does the customer have the right to direct how and for what purpose the ship is to be used throughout the period of use and whether the arrangement contains a lease?**		**6.514**
Ind AS 116 TYK-4	How would the Lessee allocate the consideration to the lease component?		**6.515**
Ind AS 116 TYK-5	What should be the lease term for lease accounting under Ind AS 116?		**6.515**
Ind AS 116 TYK-6	What should be the lease term for lease accounting under Ind AS 116?		**6.515**
Ind AS 116 TYK-7	Whether the said payments be included in the calculation of lease liability under Ind AS 116?		**6.516**
Ind AS 116 TYK-8	How will Entity X account for lease liability as at the commencement date?		**6.516**
Ind AS 116 TYK-9	How will entity X measure the right of use (ROU) asset and lease liability initially and at the end of Year 1?		**6.516**
Ind AS 12 TYK			
Ind AS 12 TYK-1	Calculate the tax base and the corresponding deferred tax or liability, if any		**9.82**
Ind AS 12 TYK-10	You are required to calculate the deferred tax arising on acquisition of Entity S. Also calculate the Goodwill arising on acquisition		**9.86**
Ind AS 12 TYK-2	Show deferred tax treatment.		**9.82**
Ind AS 12 TYK-3	Show deferred tax treatment		**9.82**
Ind AS 12 TYK-4	Calculate the Book Value as per financial and tax purposes and then DTL		**9.82**
Ind AS 12 TYK-5	Calculate deferred tax asset assuming that the carrying amount is the tax base and prepare the journal entries		**9.83**
Ind AS 12 TYK-6	Discuss the treatment of deferred tax as on 31st March, 20X1		**9.83**
Ind AS 12 TYK-7	**Explain and show how each of these events would affect the deferred tax assets / liabilities in the consolidated balance sheet of X Ltd. group at 31st March, 20X2 as per Ind AS. Assume the rate of corporate income tax is 20%**		**9.84**
Ind AS 12 TYK-8	**Explain and show how each of these events would affect the deferred tax assets / liabilities in the consolidated balance sheet of PQR Ltd. group at 31st March, 20X2 as per Ind AS. The rate of corporate income tax is 30%.**		**9.85**

Ind AS 12 TYK-9	Show the revised amount of Deferred tax asset & Deferred tax liability and present the necessary journal entries		**9.85**
Ind AS 16 TYK			
Ind AS 16 TYK-1	Advise ABC Ltd. on the costs that can be capitalized in accordance with Ind AS 16		**6.87**
Ind AS 16 TYK-10	Determine the classes of property, plant and equipment for disclosure by the entity?		**6.90**
Ind AS 16 TYK-11	Prepare machinery account in the books of Heaven Ltd. over its useful life to record the above transactions		**6.91**
Ind AS 16 TYK-2	Pass journal entries with regard to revaluation		**6.87**
Ind AS 16 TYK-3	Analyze how would the above changes in estimates be accounted by B Ltd		**6.88**
Ind AS 16 TYK-4	Determine the accounting for the above transaction for X Ltd		**6.88**
Ind AS 16 TYK-5	Examine how the entity will account for the above changes in decommissioning liability in the 11th year, if it adopts cost model		**6.88**
Ind AS 16 TYK-6	Examine how will the entity account for the above changes in decommissioning liability if it adopts revaluation model		**6.88**
Ind AS 16 TYK-7	Examine the impact of revaluation of useful life on the Statement of Profit and Loss for the year ending 31st March, 20X5		**6.89**
Ind AS 16 TYK-8	Advise the finance controller for resolving the query of the managing director?		**6.89**
Ind AS 16 TYK-9	Advise how should the company account for revaluation of plant and machinery and depreciation subsequent to revaluation. Support your answer with journal entries		**6.90**
Ind AS 19 TYK			
Ind AS 19 TYK-1	Comment whether the entity would require to recognize any liability in respect of leaves		**8.79**
Ind AS 19 TYK-2	Determine the current service cost		**8.79**
Ind AS 19 TYK-3	Compute the benefit to be attributed before the age of 25 and after 25?		**8.79**
Ind AS 19 TYK-4	State how would you measure the benefit to be attributed for the employee service for the last 20 years, 10 and 20 years and within 10 years		**8.80**
Ind AS 19 TYK-5	Determine what would be the accounting if the payment from defined contribution plan does not fall due within 12 months from the end of accounting period		**8.80**
Ind AS 19 TYK-5	State what would be the treatment of the short-term compensating absences, profit-sharing plan and the defined contribution plan in the books of Cisca Pvt. Ltd.		**8.80**
Ind AS 19 TYK-5	State what would be the treatment, if the contribution paid from defined contribution plan exceeds the contribution due.		**8.80**
Ind AS 19 TYK-6	Provide the accounting treatment in this case		**8.80**
Ind AS 19 TYK-7	Suggest if there is any amount based on the above-mentioned information that would be taken to other comprehensive income (with workings). Also compute net interest on the net defined benefit liability (asset).		**8.81**
Ind AS 19 TYK-8	Examine and present how the above event would be reported in the financial statements of A Ltd. for the year ended 31st March, 20X2 as per Ind AS. Finance cost is to be computed on the opening balances		**8.82**
Ind AS 19 TYK-9	Provide a reconciliation from the opening balance to the closing balance for plan assets and defined benefit obligation. Also show how much amount should be recognised in the statement of profit and loss, other comprehensive income and balance sheet?		**8.82**
Ind AS 2 TYK			
Ind AS 2 TYK-1	Compute the value of inventory of raw material?		**6.36**
Ind AS 2 TYK-2	Advise on provision to be made of 205 lakh included in Sundry Debtors, Finished goods and work-in-progress in the financial statement of 20X2-20X3		**6.36**

Ind AS 2 TYK-3	Determine the value inventory at the following dates:		**6.37**
Ind AS 2 TYK-4	Determine the overhead costs to be allocated to cost of goods sold and closing inventory?		**6.37**
Ind AS 2 TYK-5	Advise as if which of the above item is to be included in the cost of inventory and wants you to calculate cost of inventory as per Ind AS 2		**6.38**
Ind AS 2 TYK-6	Compute the cost of the inventory? Substantiate your answer with appropriate reasons and calculations, wherever required		**6.38**
Ind AS 20 TYK			
Ind AS 20 TYK-1	Recommend how should ABC Ltd. recognise the government grants in its books of accounts		**7.50**
Ind AS 20 TYK-2	Calculate the amount of government grant and pass necessary journal entry. Also examine how the government grant be recognised. Also state how the grant will be recognized in the statement of profit or loss assuming that the loan is to finance a depreciable asset		**7.50**
Ind AS 20 TYK-3	State whether the same is a government grant under Ind AS 20, Government Grants and Disclosure of Government Assistance? If yes, then how the same is to be accounted for if it is		**7.51**
Ind AS 20 TYK-4	State whether the accounting treatment of the grants in the nature of promoters' contribution as per AS 12 is also permitted under Ind AS 20 Accounting for Government Grants and Disclosure of Government Assistance		**7.51**
Ind AS 20 TYK-5	Suggest the accounting treatment of, if any, for the two grants received and the flood-related compensation in the books of accounts of Rainbow Limited as at 31st March, 20X2		**7.51**
Ind AS 20 TYK-6	Show the statement of profit and loss and balance sheet extracts in respect of the grant for first year under both the methods as per Ind AS 20		**7.52**
Ind AS 20 TYK-7	State, how this grant should be accounted for		**7.52**
Ind AS 20 TYK-8	Calculate the grant income and deferred income to be accounted for in the books for the years 1, 2 and 3 under the following two situations		**7.52**
Ind AS 21 TYK			
Ind AS 21 TYK-1	Calculate P's gain on disposal in its consolidated financial statements		**9.122**
Ind AS 21 TYK-2	Analyse in A's consolidated financial statements, whether the perpetual debt can be considered in accordance with para 15 of Ind AS 21, a monetary item "for which settlement is neither planned nor likely to occur in the foreseeable future" (i.e. part of A's net investment in B), with the exchange gains and losses on the perpetual debt therefore being recorded in equity?		**9.122**
Ind AS 21 TYK-3	Prepare a working of the cumulative balance of the foreign currency translation reserve		**9.123**
Ind AS 21 TYK-4	**Pass the Journal entries for the year ended on 31st March 20X1 and year 20X2 according to Ind AS 21.**		**9.123**
Ind AS 21 TYK-5	Examine the impact of this transaction on the financial statements of P Ltd. for the year ended 31st March, 20X2 as per Ind AS		**9.124**
Ind AS 21 TYK-6	**State the date of transaction for advance consideration and recognition of revenue. Also state the amount of revenue in Rupees ( ) to be recognized on the date of recognition of revenue**		**9.124**
Ind AS 21 TYK-7	Determine the unrealised profit to be eliminated in the preparation of consolidated financial statements		**9.124**
Ind AS 21 TYK-8	**Advise the appropriate accounting treatment for the foreign currency loan in the books of Makers Ltd. for the financial year 20X1-20X2. Also calculate the initial measurement amount for the loan, finance cost for the year, closing balance and exchange gain / loss**		**9.125**
Ind AS 23 TYK			

Ind AS 23 TYK-1	Advise whether it is permissible for Marine Transport Limited to capitalise any borrowing costs for the financial year ended 31st March, 20X1 or 31st March, 20X2		**6.126**
Ind AS 23 TYK-2	Compute the borrowing costs that need to be capitalised		**6.126**
Ind AS 23 TYK-3	Calculate the capitalization rate for computation of borrowing cost in accordance with Ind AS 23 'Borrowing Costs'		**6.127**
Ind AS 23 TYK-4	Calculate the amount of interest to be capitalized and pass necessary journal entry for capitalizing the cost and borrowing cost in respect of the building as on 31st January, 20X2		**6.127**
Ind AS 23 TYK-5	Determine the amount of the borrowing costs which can be capitalized at the year end as per relevant Ind AS		**6.128**
Ind AS 23 TYK-6	Compute the amount of borrowing costs eligible for capitalisation in the financial statements of each of the four entities for the current reporting period 20X1-20X2		**6.129**
Ind AS 23 TYK-7	Compute the amount of borrowing costs to be capitalized if the company amortizes discount using Effective Interest Rate method by applying 13.39% p.a. of EIR		**6.129**
Ind AS 23 TYK-8	Advice how to account for the interest paid in the books of accounts. Will your answer be different, if the whole process of renovation and modernization gets completed by 28th February, 20X2?		**6.130**
Ind AS 24 TYK			
Ind AS 24 TYK-1a	Examine when can a related party relationship is established, from the perspective of A Limited's financial statements		**10.30**
Ind AS 24 TYK-1b	Examine when can related party relationship is established, from the perspective of B Limited's financial statements		**10.30**
Ind AS 24 TYK-1c	Will A Limited and B Limited be related parties if Mr. X has only significant influence over A Limited and Ms. Y also has significant influence over B Limited		**10.30**
Ind AS 24 TYK-2a	Examine related party relationship from the perspective of C Limited's financial statements		**10.30**
Ind AS 24 TYK-2b	Examine related party relationship from the perspective of B Limited's financial statements		**10.30**
Ind AS 24 TYK-3	Analyse and show (where possible by quantifying amounts) how the above event would be reported in the financial statements of XYZ Ltd. for the year ended 31st March 20X2 as per Ind AS. You are required to mention the disclosure requirements as well.		**10.31**
Ind AS 24 TYK-4	Examine whether the sitting fee paid to independent director and non-executive director is required to be disclosed in the financial statements prepared as per Ind AS?		**10.31**
Ind AS 24 TYK-5	Provide answers to the query raised by the Managing Director Mr. Y as per Ind AS		**10.31**
Ind AS 24 TYK-6	Determine the entity to whom exemption from disclosure of related party transactions is to be given. Also examine the transactions and with whom such exemption applies		**10.31**
Ind AS 24 TYK-6	What are the disclosure requirements for the entity which has availed the exemption?		**10.31**
Ind AS 24 TYK-7	Whether the above transaction is required to be disclosed as a related party transaction as per Ind AS 24 in the financial statements of S Ltd.? What should be the disclosures in this regard?		**10.32**
Ind AS 33 TYK			
Ind AS 33 TYK-1	Calculate the number of shares for use in the EPS calculation for the calendar year		**10.90**

Ind AS 33 TYK-2	Calculate basic and diluted EPS. Ignore the need to split the convertible bonds into liability and equity elements		10.90
Ind AS 33 TYK-3	Calculate the diluted EPS for the period		10.90
Ind AS 33 TYK-4	Calculate Basic EPS for period ending 20X0, 20X1 and 20X2, when		10.91
Ind AS 33 TYK-5	Calculate Subsidiary's and Group's Basic EPS and Diluted EPS, when		10.91
Ind AS 33 TYK-6	Compute the following - the basic and diluted earnings per share for the year ended 31st March, 20X3		10.92
Ind AS 33 TYK-6	Compute the following - the finance cost of convertible debentures and its closing balance as on 31st March, 20X3 to be presented in the CFS		10.92
IND AS 34 TYK			
IND AS 34 TYK-1	Entity publishes interim financial reports half-yearly.	interim financial reports half-yearly	3.105
IND AS 34 TYK-1	Entity publishes interim financial reports quarterly	interim financial reports quarterly	3.105
IND AS 34 TYK-2	calculate the tax expense for each quarter, assuming that there is no difference between the estimated taxable income and the estimated accounting income:	Interim Quarter report - Tax Expense	3.105
IND AS 34 TYK-3	State whether the management's views are correct or not? If not, then calculate the tax expense for each quarter as well as for the year as per Ind AS 34.	Interim Quarter report - Tax Expense	3.105
IND AS 34 TYK-4	When should the loss be reported in interim statement of profit and loss of Happy India Ltd.?	Interim stt of p/L - Loss reporting	3.106
IND AS 34 TYK-5	How the related tax charge would be calculated for the year 2019 and its quarters.	Interim Quarter report - Tax charge	3.106
IND AS 34 TYK-6	**How the following transactions and events should be dealt with while preparing its interim financials:**	**Interim stt of p/L - recog & meas principles**	3.106
Ind AS 36 TYK			
Ind AS 36 TYK-1	Determine the CGU of the building		6.198
Ind AS 36 TYK-10	Calculate expected cash flows in each of the following cases		6.200
Ind AS 36 TYK-11a	Compute the impairment loss on CGU and carrying value of each asset after charging impairment loss for the year ending 31st March, 20X8 by providing all the relevant working notes to arrive at such calculation		6.201
Ind AS 36 TYK-11b	Compute the prospective depreciation for the year 20X8-20X9 on the above assets		6.202
Ind AS 36 TYK-11c	Compute the carrying value of CGU as at 31st March, 20X9		6.202
Ind AS 36 TYK-12	Determine the value in use of the machine in accordance with Ind AS 36?		6.202
Ind AS 36 TYK-13	Calculate impairment loss, if any and revised depreciation of asset. Also suggest how Impairment loss, if any would be set off and how compensation from government be accounted for?		6.203
Ind AS 36 TYK-14	Calculate - The carrying amount of the machine on 31st December Year 3 (immediately before the impairment)		6.203
Ind AS 36 TYK-2	Calculate the impairment loss, if any. Ignore decimals		6.199
Ind AS 36 TYK-3	Allocate the impairment loss on 31st March, 20X2		6.199
Ind AS 36 TYK-4	Calculate the impairment loss, if any		6.199
Ind AS 36 TYK-5	Advise, how it should deal with under Ind AS 36		6.199
Ind AS 36 TYK-6	Calculate the amount of impairment loss or its reversal, if any, on 31st March, 20X1, 31st March, 20X2 and 31st March, 20X3		6.200
Ind AS 36 TYK-7	Calculate value in use as on 31st March, 20X1		6.200
Ind AS 36 TYK-8	Calculate expected cash flows		6.200
Ind AS 36 TYK-9	Calculate expected cash flows assuming applicable discount rate of 5%, 5.25% and 5.5% in year 1, 2 and 3, respectively		6.200

Ind AS 37 TYK			
Ind AS 37 TYK-1	Advise how the company should account for these transactions in the financial year 20X1-20X2		8.133
Ind AS 37 TYK-2	State the nature of obligation that the entity has in such a case		8.133
Ind AS 37 TYK-3	Determine the provisions that the Company is required to make as per Ind AS 37		8.134
Ind AS 37 TYK-4	Identify the treatment of duty drawback credit as per the given information		8.134
Ind AS 37 TYK-5	Evaluate whether the contract is onerous and also determine the amount of provision to be made in this regard		8.135
Ind AS 37 TYK-6	Calculate the amount to be provided at 31st March 20X2 for the restoration costs		8.135
Ind AS 38 TYK			
Ind AS 38 TYK-1	Determine how the above transactions be accounted for by X Ltd		6.276
Ind AS 38 TYK-10	Advise how the entity should account for the above cost incurred on promoting such show		6.278
Ind AS 38 TYK-11	Tabulate the accounting treatment of expenditure incurred in 20X1-20X2 and 20X2-20X3 as per relevant Ind AS. Ignore effects of amortisation		6.279
Ind AS 38 TYK-12	Interpret how X Ltd. should account for the above-mentioned cost		6.279
Ind AS 38 TYK-13	Determine how X Ltd. should account for the development expenditure		6.279
Ind AS 38 TYK-14	Analyse how should X Ltd. account for the revalued intangible assets in its books of account		6.279
Ind AS 38 TYK-15	Advise the appropriate accounting treatment for the aforesaid issue for the year ended 31st March, 20X6		6.280
Ind AS 38 TYK-2	Advise whether the franchise rights be treated as an intangible asset under Ind AS 38		6.276
Ind AS 38 TYK-3	Evaluate whether the customer list be treated as an intangible asset under Ind AS 38		6.277
Ind AS 38 TYK-4	Advise X Ltd. on the above issue		6.277
Ind AS 38 TYK-5	Recommend the cost of acquisition to be capitalised as an intangible asset under Ind AS 38		6.277
Ind AS 38 TYK-6	Identify at what cost the intangible asset will be recognized		6.277
Ind AS 38 TYK-7	Recommend how would X Limited account for the net assets acquired from Y Limited		6.277
Ind AS 38 TYK-8	Determine at what amount the intangible asset be measured under Ind AS 38		6.278
Ind AS 38 TYK-9	Compute the value of patent right for initial recognition in the books of X Ltd. in following two situations		6.278
Ind AS 40 TYK			
Ind AS 40 TYK-1	What is the carrying amount of the building on 31st March, 20X2?		6.312
Ind AS 40 TYK-2	How should X Limited account for the above investment property as on 31st March, 20X1?		6.312
Ind AS 40 TYK-3	How X Limited will account for all the above-mentioned expenses in the books of account?		6.313
Ind AS 40 TYK-4	Examine and show how the three events would be reported in the financial statements of X Ltd. for the year ended 31st March, 20X6 as per Ind AS		6.313
Ind AS 40 TYK-5	What would be the treatment of Building A and Building B in the balance sheet of Shaurya Limited? Provide detailed disclosures and computations in line with relevant Indian accounting standards. Treat it as if you are preparing a separate note or schedule, of the given assets in the balance sheet		6.314
Ind AS 40 TYK-6a	How should the land property be classified by X Ltd in its financial statements as at 31st March 20X2?		6.315

Ind AS 40 TYK-6b	Will there be a change in the carrying amount of the property resulting from any change in use of the investment property?		**6.315**
Ind AS 40 TYK-6c	Whether the change in classification to, or from, investment properties is a change in accounting policy to be accounted for in accordance with Ind AS 8, Accounting Policies, Changes in Accounting Estimates and Errors?		**6.315**
Ind AS 40 TYK-6d	Would your answer to (a) above be different if there were to be a management intention to commence construction of an office building for own use; however, no construction activity was planned by 31st March 20X2?		**6.315**
Ind AS 41 TYK			
Ind AS 41 TYK-1	Calculate the amount at which cattle is to be recognised in books on initial recognition and at year end 31st March, 20X2. Show corresponding journal entries.		**7.22**
Ind AS 41 TYK-2	Pass necessary journal entries of above transactions with respect to cows in the financial statements of XY Ltd. for the year ended 31st March, 20X2? Also show the amount lying in inventory if any		**7.23**
Ind AS 41 TYK-3	Pass Journal entries for the initial and subsequent measurement for all above transactions. Interim reporting periods are of 30th September and 31 March and the company determines the fair values on these dates for reporting		**7.23**
Ind AS 41 TYK-4	Also pass journal entries under both the situations on both dates		**7.24**
Ind AS 41 TYK-4	Analyse whether the following activities fall within the scope of Ind AS 41 with proper reasoning		**7.24**
Ind AS 41 TYK-4	Determine the fair value on the date of purchase and as on financial year ended 31st March, 20X2 under both the cases viz		**7.24**
Ind AS 7 TYK			
Ind AS 7 TYK-1	Use the following data of ABC Ltd. to construct a statement of cash flows using the direct and indirect methods:	direct and indirect methods	**3.156**
Ind AS 7 TYK-2	From the following summary cash account of XYZ Ltd, prepare cash flow statement for the year ended March 31, 20X1 in accordance with Ind AS 7 using direct method.	direct methods	**3.157**
Ind AS 7 TYK-3	How these transactions should be presented in cash flow for the year ended 31.12.20X2 as per Ind AS 7?	Foreign Txn in stt of Cash flow	**3.157**
Ind AS 7 TYK-4	Advise how the above transactions will be disclosed/presented in the statement of cash flows as per Ind AS 7.	Control of Subsi - Stt of Cash Flow	**3.158**
Ind AS 7 TYK-5	Prepare the Consolidated Statement of Cash Flows for the year 20X2	Consolidated Stt of cash flow	**3.159**
Ind AS 7 TYK-6	You need to determine the net cash flow from operating activities, investing activities and financing activities of Akola Limited	Net cash flow from operating activities	**3.159**
Ind AS 7 TYK-7	Prepare statement of cash flows showing cash generated from Operating Activities using direct method	cash generated from Operating Activities - Direct method	**3.159**
Ind AS 7 TYK-8	What will be the classification for following items in the statement of cash flows of both (i) Banks / Financial institutions and (ii) Other Entities?	classification of items	**3.160**
Ind AS 8 TYK			
Ind AS 8 TYK-1	Whether this change in recognising the revenue is a change in accounting policy as per the provision of Ind AS 8?	Change in recognising revenue	**4.41**
Ind AS 8 TYK-10	State how the above will be treated /accounted in Cheery Limited's Statement of profit and loss, statement of changes in equity and in notes wherever required for current period and earlier period(s) as per relevant Ind AS.	Item added incorrectly in inventory	**4.44**
Ind AS 8 TYK-11	Analyse the above situation in accordance with relevant Ind AS.	Change in A/c Est - Latent defect identified	**4.44**
Ind AS 8 TYK-2	Under what circumstances an entity is required to present a third balance sheet at the beginning of the preceding period?	Third Balance sheet - under what circumstances	**4.41**

Ind AS 8 TYK-3	You are required to prepare the relevant note for disclosure in accordance with Ind AS 8	Disclosure -PPE, Depreciation	**4.42**
Ind AS 8 TYK-4	Is change in the depreciation method for an item of property, plant and equipment a change in accounting policy or a change in accounting estimate?	Change in Depreciation method	**4.42**
Ind AS 8 TYK-5	Would this reclassification of expenses from finance costs to other expenses in the comparative amounts will be considered as correction of an error under Ind AS 8? Would the entity need to present a third balance sheet?	Reclassification of expense	**4.42**
Ind AS 8 TYK-6	Would this situation require retrospective restatement of comparatives considering that the amount was material?	retrospective restatement of comparatives	**4.43**
Ind AS 8 TYK-7	Whether the management's view is acceptable?	Under-accrual of exp - immaterial to annual FS	**4.43**
Ind AS 8 TYK-8	How should the error be corrected in the financial statements for the year ended 31st March, 20X4, assuming the impact of the same is considered material? For simplicity, ignore tax effects	Error - Inv Prop not depreciated	**4.43**
Ind AS 8 TYK-9	You are required to present the impact of change in accounting policy in the profit or loss and produce an extract of the statement of changes in equity in accordance with Ind AS 8	Change in A/c Policy - FIFO to Wtd Avg	**4.44**
PROFESSIONAL & ETHICAL DUTY OF CA TYK			
PROFESSIONAL & ETHICAL DUTY OF CA TYK-1	Discuss the potential ethical conflicts which may arise in the above scenario and the ethical principles which would guide how the financial controller should respond to the situation		**16.43**

TEST YOUR KNOWLEDGE

Question

1. The directors of Jayant Ltd. have received the following email from its majority shareholder:

   To: Directors of Jayant Ltd.

   Re: Measurement

   I recently read an article published in the financial press about the 'mixed measurement approach' that is used by lots of companies. I hope Jayant Ltd. does not follow such an approach because 'mixed' seems to imply 'inconsistent'. I believe that consistency is of paramount importance, and hence feel it would be better to measure everything in a uniform manner. It would be appreciated if you could provide further information at the next annual general meeting on measurement bases, covering what approach is taken by Jayant Ltd. and why, and the potential effect such an approach has on the investors trying to analyse the financial statements.

   Prepare notes for the directors of Jayant Ltd. to discuss the issue raised in the shareholders' email with reference to the Conceptual Framework wherever appropriate.

Answer

1. 'Mixed measurement' approach implies that a company selects different measurement bases (e.g. historical cost or fair value) for its various assets and liabilities, rather than using one single measurement basis for all items. The measurement basis so selected should reflect the type of entity and the sector in which it operates and the business model that the entity adopts.

   There are criticisms of the mixed measurement approach, particularly under the IFRS regime, because investors think that if different measurement bases are used for assets and liabilities, the resulting figures could lack relevance or exhibit little meaning.

   It is however important to note that figures of items in the financial statements cannot be derived by following a one-size-fits-all approach. Such an approach may not provide relevant information to users. A particular measurement basis may be easier to understand, more verifiable and less costly to implement. Therefore, to state that 'mixed measurement' approach is 'inconsistent' is a poor argument. In reality, a mixed approach may actually provide more relevant information to the stakeholders.

   The Conceptual Framework confirms the allowance of the usage of a mixed measurement approach in developing standards. The measurement methods included in the standards are

© The Institute of Chartered Accountants of India

those which the standard-setters believe provide the most relevant information and which most faithfully represent the underlying transaction or event. Based on the reactions to the convergence to Ind AS, it feels that most investors feel this approach is consistent with their analysis of financial statements. Thus, the arguments against a mixed measurement are far outweighed by the greater relevance achieved by such measurement bases.

Jayant Ltd. prepares its financial statements under Ind AS, and therefore applies the measurement bases permitted in Ind AS. Ind AS adopt a mixed measurement basis, which includes current value (fair value, value in use, fulfilment value and current cost) and historical cost.

Where an Ind AS allows a choice of measurement basis, the directors of Jayant Ltd. must exercise judgment as to which basis will provide the most useful information for its primary users. Furthermore, when selecting a measurement basis, measurement uncertainty should also be considered. The Conceptual Framework states that for some estimates, a high level of measurement uncertainty may outweigh other factors to such an extent that the resulting information may be of little relevance.

© The Institute of Chartered Accountants of India

FOR SHORTCUT TO IND AS WISDOM: SCAN ME!

TEST YOUR KNOWLEDGE

Questions

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

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

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

2. In December 20X1 an entity entered into a loan agreement with a bank. The loan is repayable in three equal annual instalments starting from December 20X5. One of the loan covenants is that an amount equivalent to the loan amount should be contributed by promoters by 24th March, 20X2, failing which the loan becomes payable on demand. As on 24th March, 20X2, the entity has not been able to get the promoter's contribution. On 25th March, 20X2, the entity approached the bank and obtained a grace period upto 30th June, 20X2 to get the promoter's contribution.

   The bank cannot demand immediate repayment during the grace period. The annual reporting period of the entity ends on 31st March.

   (a) As on 31st March, 20X2, how should the entity classify the loan?

   (b) Assume that in anticipation that it may not be able to get the promoter's contribution by due date, in February 20X2, the entity approached the bank and got the compliance

© The Institute of Chartered Accountants of India

date extended upto 30th June, 20X2 for getting promoter's contribution. In this case will the loan classification as on 31st March, 20X2 be different from (a) above?

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

   Advise on the classification of the liability as current / non-current.

4. Entity A has undertaken various transactions in the financial year ended 31st March, 20X1. Identify and present the transactions in the financial statements as per Ind AS 1. ₹

	₹
Remeasurement of defined benefit plans	2,57,000
Current service cost	1,75,000
Changes in revaluation surplus	1,25,000
Gains and losses arising from translating the monetary assets in foreign currency	75,000
Gains and losses arising from translating the financial statements of a foreign operation	65,000
Gains and losses from investments in equity instruments designated at fair value through other comprehensive income	1,00,000
Income tax expense	35,000
Share based payments cost	3,35,000

5. XYZ Limited (the 'Company') is into the manufacturing of tractor parts and mainly supplying components to the Original Equipment Manufacturers (OEMs). The Company does not have any subsidiary, joint venture or associate company. During the preparation of financial statements for the year ended 31st March, 20X1, the accounts department is not sure about the treatment / presentation of below mentioned matters. Accounts department approached you to advice on the following matters.

S. No.	Matters
(i)	There are qualifications in the audit report of the Company with reference to two Ind AS.

© The Institute of Chartered Accountants of India

(ii)	Is it mandatory to add the word "standalone" before each of the components of financial statements?
(iii)	The Company is Indian Company and preparing and presenting its financial statements in ₹. Is it necessary to write in the financial statements that the financial statements have been presented in ₹.
(iv)	The Company had sales transactions with 10 related party parties during previous year. However, during current year, there are no transactions with 4 related parties out of aforesaid 10 related parties. Hence, Company is of the view that it need not disclose sales transactions with these 4 parties in related party disclosures because with these parties there are no transactions during current year.

Evaluate the above matters with respect to preparation and presentation of a general-purpose financial statement.

6. A Company presents financial results for three years (i.e., one for current year and two comparative years) internally for the purpose of management information every year in addition to the general-purpose financial statements. The aforesaid financial results are presented without furnishing the related notes because these are not required by the management for internal purposes. During the current year, management thought why not they should present third year statement of profit and loss also in the general-purpose financial statements. It will save time and will be available easily whenever management needs this in future.

   With reference to above background, answer the following:

   (i) Can management present the third statement of profit and loss as an additional comparative in the general-purpose financial statements?

   (ii) If management present third statement of profit and loss in the general-purpose financial statement as comparative, is it necessary that this statement should- be compliant of Ind AS?

   (iii) Can management present third statement of profit and loss only as additional comparative in the general-purpose financial statements without furnishing other components (like balance sheet, statement of cash flows, statement of change in equity) of financial statements?

7. A company, while preparing the financial statements for financial year 20X1-20X2, erroneously booked excess revenue of ₹ 10 crore. The total revenue reported in financial year 20X1-20X2 was ₹ 80 crore. However, while preparing the financial statements for 20X2-20X3, it discovered that excess revenue was booked in financial year 20X1-20X2 which

© The Institute of Chartered Accountants of India

it now wants to correct in the financial statements. However, the management of the company is not sure whether it need to present the third balance sheet as additional comparative.

With regard to the above background, answer the following:

(i) Is it necessary to provide the third balance sheet at the beginning of the preceding period in this case?

(ii) The company wants to correct the errors during financial year 20X2-20X3 by giving impact in the figures of current year only. Is the contention of the management, correct?

8. XYZ Limited (the 'Company') is into construction of turnkey projects and has assessed its operating cycle to be 18 months. The Company has certain trade receivables and payables which are receivable and payable within a period of twelve months from the reporting date, i.e., 31st March, 20X2.

In addition to above there are following items/transactions which took place during financial year 20X1-20X2:

S. No.	Items/transactions
(1)	The company has some trade receivables which are due after 15 months from the date of the balance sheet. So, the company expects that the payment will be received within the period of operating cycle.
(2)	The company has some trade payables which are due for payment after 14 months from the date of balance sheet. These payables fall due within the period of operating cycle. Though the company does not expect that it will be able to pay these payables within the operating cycle because the nature of business is such that generally projects get delayed and payments from customers also get delayed.
(3)	The company was awarded a contract of ₹ 100 crore on 31st March, 20X2. As per the terms of the contract, the company made a security deposit of 5% of the contract value with the customer, of ₹ 5 crore on 31st March, 20X2. The contract is expected to be completed in 18 months' time. The aforesaid deposit will be refunded back after 6 months from the date of the completion of the contract.
(4)	The company has also given certain contracts to third parties and have received security deposits from them of ₹ 2 crore on 31st March, 20X2 which are repayable on completion of the contract but if contract is cancelled before the

© The Institute of Chartered Accountants of India

	contract term of 18 months, then it becomes payable immediately. However, the Company does not expect the cancellation of the contract.

Considering the above items/transactions answer the following:

(i) The company wants to present the trade receivable as current despite the fact that these are receivables in 15 months' time. Does the decision of presenting the same as current is correct?

(ii) The company wants to present the trade payables as non-current despite the fact that these are due within the operating cycle of the company. Does the decision of presenting the same as non-current is correct?

(iii) Can the security deposit of ₹ 5 crore made by the company with the customers be presented as current?

(iv) Can the security deposit of ₹ 2 crore taken by the company from contractors be presented as non-current?

9. Is offsetting permitted under the following circumstances?

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

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

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

Answers

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

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

© The Institute of Chartered Accountants of India

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

2. (a) Ind AS 1, inter alia, provides, "An entity classifies the liability as non-current if the lender agreed by the end of the reporting period to provide a period of grace ending at least twelve months after the reporting period, within which the entity can rectify the breach and during which the lender cannot demand immediate repayment." In the present case, following the default, grace period within which an entity can rectify the breach is less than twelve months after the reporting period. Hence as on 31st March, 20X2, the loan will be classified as current.

(b) Ind AS 1 deals with classification of liability as current or non-current in case of breach of a loan covenant and does not deal with the classification in case of expectation of breach. In this case, whether actual breach has taken place or not is to be assessed on 30th June, 20X2, i.e., after the reporting date. Consequently, in the absence of actual breach of the loan covenant as on 31st March, 20X2, the loan will retain its classification as non-current.

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

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

In the given case, Company B (the lender) agreed for not to demand payment but only after the reporting date and the financial statements were approved for issuance. The financial statements were approved for issuance in the month of June 20X2 and both companies agreed for not to demand payment in the month of July 20X2 although negotiation started in the month of May 20X2 but could not agree before June 20X2 when financial statements were approved for issuance.

© The Institute of Chartered Accountants of India

Hence, the liability should be classified as current in the financial statement as at 31st March, 20X2.

4. Items impacting the Statement of Profit and Loss for the year ended 31st March, 20X1 (₹)

Current service cost	1,75,000
Gains and losses arising from translating the monetary assets in foreign currency	75,000
Income tax expense	35,000
Share based payments cost	3,35,000

Items impacting the other comprehensive income for the year ended 31st March, 20X1 (₹)

Remeasurement of defined benefit plans	2,57,000
Changes in revaluation surplus	1,25,000
Gains and losses arising from translating the financial statements of a foreign operation	65,000
Gains and losses from investments in equity instruments designated at fair value through other comprehensive income	1,00,000

5. (i) Yes, an entity whose financial statements comply with Ind AS shall make an explicit and unreserved statement of such compliance in the notes. An entity shall not describe financial statements as complying with Ind AS unless they comply with all the requirements of Ind AS. (Refer Para 16 of Ind AS 1)

(ii) No, but need to disclose in the financial statement that these are individual financial statements of the Company. (Refer Para 51(b) of Ind AS 1)

(iii) Yes, Para 51(d) of Ind AS 1 inter alia states that an entity shall display the presentation currency, as defined in Ind AS 21 prominently, and repeat it when necessary for the information presented to be understandable.

(iv) No, as per Para 38 of Ind AS 1, except when Ind AS permit or require otherwise, an entity shall present comparative information in respect of the preceding period for all amounts reported in the current period's financial statements. An entity shall include comparative information for narrative and descriptive information if it is relevant to understanding the current period's financial statements.

© The Institute of Chartered Accountants of India

6. (i) Yes, as per Para 38C of Ind AS 1, an entity may present comparative information in addition to the minimum comparative financial statements required by Ind AS, as long as that information is prepared in accordance with Ind AS. This comparative information may consist of one or more statements referred to in paragraph 10 but need not comprise a complete set of financial statements. When this is the case, the entity shall present related note information for those additional statements.

(ii) Yes, as per Para 38C of Ind AS 1, an entity may present comparative information in addition to the minimum comparative financial statements required by Ind AS, as long as that information is prepared in accordance with Ind AS.

(iii) Yes, as per Para 38C of Ind AS 1, an entity may present comparative information in addition to the minimum comparative financial statements required by Ind AS, as long as that information is prepared in accordance with Ind AS. This comparative information may consist of one or more statements referred to in paragraph 10 but need not comprise a complete set of financial statements. When this is the case, the entity shall present related note information for those additional statements.

7. (i) No, as per Para 40A of Ind AS 1, an entity shall present a third balance sheet as at the beginning of the preceding period in addition to the minimum comparative financial statements required in paragraph 38A if:

(a) it applies an accounting policy retrospectively, makes a retrospective restatement of items in its financial statements or reclassifies items in its financial statements; and

(b) the retrospective application, retrospective restatement or the reclassification has a material effect on the information in the balance sheet at the beginning of the preceding period.

(ii) No, management need to correct the previous year figures to correct the error but need not to furnish third balance sheet at the beginning of preceding period. (Refer Para 40A of Ind AS 1)

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

(ii) No, the Company cannot disclose these payables as non-current and the Company also need to disclose amounts that are payable within a period of 12 months and after 12 months from the reporting date. (Refer Para 60 and 61 of Ind AS 1)

© The Institute of Chartered Accountants of India

(iii) No, because the amount will be received after the operating cycle of the Company. (Refer Para 66 of Ind AS 1)

(iv) No, because the amount may be required to be paid before completion of the contract in case the contract is cancelled. (Refer Para 69 of Ind AS 1).

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

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

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

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

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

© The Institute of Chartered Accountants of India

FOR SHORTCUT TO IND AS WISDOM: SCAN ME!

TEST YOUR KNOWLEDGE

Questions

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

   (i) Entity publishes interim financial reports quarterly

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

2. Narayan Ltd. provides you the following information and asks you to calculate the tax expense for each quarter, assuming that there is no difference between the estimated taxable income and the estimated accounting income:

Estimated Gross Annual Income (inclusive of Estimated Capital Gains of ₹ 8,00,000)	33,00,000

   Estimated Income of Quarter I is ₹ 7,00,000, Quarter II is ₹ 8,00,000, Quarter III (including Estimated Capital Gains of ₹ 8,00,000) is ₹ 12,00,000 and Quarter IV is ₹ 6,00,000.

Tax Rates:	On Capital Gains	12%
	On Other Income: First ₹ 5,00,000	30%
	Balance Income·	40%

3. An entity reports quarterly, earns ₹ 1,50,000 pre-tax profit in the first quarter but expects to incur losses of ₹ 50,000 in each of the three remaining quarters. The entity operates in a jurisdiction in which its estimated average annual income tax rate is 30%.

   The management believes that since the entity has zero income for the year, its income-tax expense for the year will be zero. State whether the management's views are correct or

© The Institute of Chartered Accountants of India

not? If not, then calculate the tax expense for each quarter as well as for the year as per Ind AS 34.

4. Due to decline in market price in second quarter, Happy India Ltd. incurred an inventory loss. The Market price is expected to return to previous levels by the end of the year. At the end of year, the decline had not reversed. When should the loss be reported in interim statement of profit and loss of Happy India Ltd.?

5. An entity's accounting year ends is 31st December, but its tax year end is 31st March. The entity publishes an interim financial report for each quarter of the year ended 31st December, 2019. The entity's profit before tax is steady at ₹10,000 each quarter, and the estimated effective tax rate is 25% for the year ended 31st March, 2019 and 30% for the year ended 31st March, 2020.

   How the related tax charge would be calculated for the year 2019 and its quarters.

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

   (i) It makes employer contributions to government-sponsored insurance funds that are assessed on an annual basis. During Quarter 1 and Quarter 2 larger amount of payments for this contribution were made, while during the Quarter 3 minor payments were made (since contribution is made upto a certain maximum level of earnings per employee and hence for higher income employees, the maximum income reaches before year end).

   (ii) The entity intends to incur major repair and renovation expense for the office building. For this purpose, it has started seeking quotations from vendors. It also has tentatively identified a vendor and expected costs that will be incurred for this work.

   (iii) The company has a practice of declaring bonus of 10% of its annual operating profits every year. It has a history of doing so.

Answers

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

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

a) balance sheet as of the end of the current interim period and a comparative balance sheet as of the end of the immediately preceding financial year.

b) statements of profit and loss for the current interim period and cumulatively for the current financial year to date, with comparative statements of profit and loss for the

© The Institute of Chartered Accountants of India

comparable interim periods (current and year-to-date) of the immediately preceding financial year.

c) statement of changes in equity cumulatively for the current financial year to date, with a comparative statement for the comparable year-to-date period of the immediately preceding financial year.

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

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

(i) Entity publishes interim financial reports quarterly

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

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

(ii) Entity publishes interim financial reports half-yearly

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

Balance sheet at	**30th September, 20X1**	**31st March, 20X1**
Statement of profit and loss for	6 months ending 30th September, 20X1	6 months ending 30th September, 20X0

© The Institute of Chartered Accountants of India

Statement of changes in equity for	6 months ending 30th September 20X1	6 months ending 30th September 20X0
Statement of cash flows for	6 months ending 30th September 20X1	6 months ending 30th September 20X0

2. As per para 30(c) of Ind AS 34 'Interim Financial Reporting', income tax expense is recognised in each interim period based on the best estimate of the weighted average annual income tax rate expected for the full financial year.

If different income tax rates apply to different categories of income (such as capital gains or income earned in particular industries) to the extent practicable, a separate rate is applied to each individual category of interim period pre-tax income.

	₹
Estimated annual income exclusive of estimated capital gain (33,00,000 – 8,00,000) (A)	25,00,000
Tax expense on other income:	
30% on ₹ 5,00,000	1,50,000
40% on remaining ₹ 20,00,000	8,00,000
(B)	9,50,000
Weighted average annual income tax rate = $\frac{B}{A} = \frac{9,50,000}{25,00,000} = 38\%$	

Tax expense to be recognised in each of the quarterly reports

		₹
Quarter I - ₹ 7,00,000 x 38%		2,66,000
Quarter II - ₹ 8,00,000 x 38%		3,04,000
Quarter III - ₹ (12,00,000 - 8,00,000) x 38%	1,52,000	
₹ 8,00,000 x 12%	96,000	2,48,000
Quarter IV - ₹ 6,00,000 x 38%		2,28,000
		10,46,000

© The Institute of Chartered Accountants of India

3. As illustrated in para 30 (c) of Ind AS 34 'Interim financial reporting', income tax expense is **recognised in each interim period** based on the best estimate of the weighted average annual income tax rate expected for the full financial year.

Accordingly, the management's contention that since the net income for the year will be zero no income tax expense shall be charged quarterly in the interim financial report, is not correct. Since the effective tax rate or average annual income tax rate is already given in the question as 30%, the income tax expense will be recognised in each interim quarter based on this rate only. The following table shows the correct income tax expense to be reported each quarter in accordance with Ind AS 34:

Period	Pre-tax earnings (in ₹)	Effective tax rate	Tax expense (in ₹)
First Quarter	1,50,000	30%	45,000
Second Quarter	(50,000)	30%	(15,000)
Third Quarter	(50,000)	30%	(15,000)
Fourth Quarter	(50,000)	30%	(15,000)
Annual	**0**		**0**

4. Loss should be recognised in the second quarter of the year.

5. **Table showing computation of tax charge:**

	Quarter ending 31st March, 2019	Quarter ending 30th June, 2019	Quarter ending 30th September, 2019	Quarter ending 31st December, 2019	Year ending 31st December, 2019
	₹	₹	₹	₹	₹
Profit before tax	10,000	10,000	10,000	10,000	40,000
Tax charge	(2,500)	(3,000)	(3,000)	(3,000)	(11,500)
	7,500	7,000	7,000	7,000	28,500

Since an entity's accounting year is not same as the tax year, more than one tax rate might apply during the accounting year. Accordingly, the entity should apply the effective tax rate for each interim period to the pre-tax result for that period.

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

© The Institute of Chartered Accountants of India

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

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

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

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

(ii) The cost of a planned overhaul expenditure that is expected to occur in later part of the year is not anticipated for interim reporting purposes unless an event has caused the entity to have a legal or constructive obligation. The mere intention or necessity to incur expenditure related to the future is not sufficient to give rise to an obligation.

(iii) A bonus is anticipated for interim reporting purposes, if and only if,

    (a) the bonus is a legal obligation or past practice would make the bonus a constructive obligation for which the entity has no realistic alternative but to make the payments, and

    (b) a reliable estimate of the obligation can be made. Ind AS 19, Employee Benefits provides guidance in this regard.

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

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

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

© The Institute of Chartered Accountants of India

FOR SHORTCUT TO IND AS WISDOM: SCAN ME!

TEST YOUR KNOWLEDGE

Questions

1. Use the following data of ABC Ltd. to construct a statement of cash flows using the direct and indirect methods: (Amount in ₹)

	20X2	20X1
Cash	4,000	14,000
Accounts Receivable	25,000	32,500
Prepaid Insurance	5,000	7,000
Inventory	37,000	34,000
Fixed Assets	3,16,000	2,70,000
Accumulated Depreciation	(45,000)	(30,000)
Total Assets	3,42,000	3,27,500
Accounts Payable	18,000	16,000
Wages Payable	4,000	7,000
Debentures	1,73,000	1,60,000
Equity Shares	88,000	84,000
Retained Earnings	59,000	60,500
Total Liabilities & Equity	3,42,000	3,27,500
	20X2	
Sales	2,00,000	
Cost of Goods Sold	(1,23,000)	

© The Institute of Chartered Accountants of India

Depreciation	(15,000)	
Insurance Expense	(11,000)	
Wages	(50,000)	
Net Profit	1,000	

During the financial year 20X2 company ABC Ltd. declared and paid dividend of ₹ 2,500.

During 20X2, ABC Ltd. paid ₹ 46,000 in cash to acquire new fixed assets. The accounts payable was used only for inventory. No debt was retired during 20X2.

2. From the following summary cash account of XYZ Ltd, prepare cash flow statement for the year ended March 31, 20X1 in accordance with Ind AS 7 using direct method.

Summary of Bank Account for the year ended March 31, 20X1

	₹ '000		₹ '000
Balance on 1.4.20X0	50	Payment to creditors	2,000
Issue of Equity Shares	300	Purchase of Fixed Assets	200
Receipts from customers	2,800	Overhead Expenses	200
Sale of Fixed Assets	100	Payroll	100
		Tax Payment	250
		Dividend	50
		Repayment of Bank loan	300
		Balance on 31.3.20X1	150
	3,250		3,250

3. Z Ltd. has no foreign currency cash flow for the year 20X1. It holds some deposit in a bank in the USA. The balances as on 31.12.20X1 and 31.12.20X2 were US$ 100,000 and US$ 102,000 respectively. The exchange rate on December 31, 20X1 was US$1 = ₹ 45. The same on 31.12.20X2 was US$1 = ₹ 50. The increase in the balance was on account of interest credited on 31.12.20X2. Thus, the deposit was reported at ₹ 45,00,000 in the balance sheet as on December 31, 20X1. It was reported at ₹ 51,00,000 in the balance sheet as on 31.12.20X2. How these transactions should be presented in cash flow for the year ended 31.12.20X2 as per Ind AS 7?

4. Company A acquires 70% of the equity stake in Company B on July 20, 20X1. The consideration paid for this transaction is as below:

   (a) Cash consideration of ₹ 15,00,000

   (b) 200,000 equity shares having face of ₹ 10 and fair value of ₹ 15 per share.

© The Institute of Chartered Accountants of India

On the date of acquisition, Company B has cash and cash equivalent balance of ₹ 2,50,000 in its books of account.

On October 10, 20X2, Company A further acquires 10% stake in Company B for cash consideration of ₹ 8,00,000.

Advise how the above transactions will be disclosed/presented in the statement of cash flows as per Ind AS 7.

5. Entity A acquired a subsidiary, Entity B, during the year. Summarised information from the Consolidated Statement of Profit and Loss and Balance Sheet is provided, together with some supplementary information.

Consolidated Statement of Profit and Loss

	Amount (₹)
Revenue	3,80,000
Cost of sales	(2,20,000)
Gross profit	1,60,000
Depreciation	(30,000)
Other operating expenses	(56,000)
Interest cost	(4,000)
Profit before taxation	**70,000**
Taxation	(15,000)
Profit after taxation	**55,000**

Consolidated balance sheet

	20X2	**20X1**
Assets	**Amount (₹)**	**Amount (₹)**
Cash and cash equivalents	8,000	5,000
Trade receivables	54,000	50,000
Inventories	30,000	35,000
Property, plant and equipment	1,60,000	80,000
Goodwill	18,000	—
Total assets	**2,70,000**	**1,70,000**
Liabilities		
Trade payables	68,000	60,000

© The Institute of Chartered Accountants of India

Income tax payable	12,000	11,000
Long term debt	1,00,000	64,000
Total liabilities	**1,80,000**	**1,35,000**
Shareholders' equity	**90,000**	**35,000**
Total liabilities and shareholders'	**2,70,000**	**1,70,000**

Other information

All of the shares of entity B were acquired for ₹ 74,000 in cash. The fair values of assets acquired and liabilities assumed were:

Particulars	Amount (₹)
Inventories	4,000
Trade receivables	8,000
Cash	2,000
Property, plant and equipment	1,10,000
Trade payables	(32,000)
Long term debt	(36,000)
Goodwill	18,000
Cash consideration paid	**74,000**

Prepare the Consolidated Statement of Cash Flows for the year 20X2, as per Ind AS 7.

6. During the financial year 2019-2020, Akola Limited have paid various taxes & reproduced the below mentioned records for your perusal:

   - Capital gain tax of ₹ 20 crore on sale of office premises at a sale consideration of ₹ 100 crore.
   - Income Tax of ₹ 3 crore on Business profits amounting ₹ 30 crore (assume entire business profit as cash profit).
   - Dividend Distribution Tax of ₹ 2 crore on payment of dividend amounting ₹ 20 crore to its shareholders.
   - Income tax Refund of ₹ 1.5 crore (Refund on taxes paid in earlier periods for business profits).

   You need to determine the net cash flow from operating activities, investing activities and financing activities of Akola Limited as per relevant Ind AS.

7. From the following data of Galaxy Ltd., prepare statement of cash flows showing cash generated from Operating Activities using direct method as per Ind AS 7:

© The Institute of Chartered Accountants of India

	31.3.20X2 (₹)	31.3.20X1 (₹)
Current Assets:		
Inventory	1,20,000	1,65,000
Trade receivables	2,05,000	1,88,000
Cash & cash equivalents	35,000	20,500
Current Liabilities:		
Trade payable	1,95,000	2,15,000
Provision for tax	48,000	65,000

Summary of Statement of Profit and Loss		₹
Sales	85,50,000	
Less: Cost of sales	(56,00,000)	29,50,000
Other Income		
Interest income	20,000	
Fire insurance claim received	1,10,000	1,30,000
		30,80,000
Depreciation	(24,000)	
Administrative and selling expenses	(15,40,000)	
Interest expenses	(36,000)	
Foreign exchange loss	(18,000)	(16,18,000)
Net Profit before tax and extraordinary income		14,62,000
Income Tax		(95,000)
Net Profit		13,67,000

Additional information:

(i) Trade receivables and Trade payables include amounts relating to credit sale and credit purchase only.

(ii) Foreign exchange loss represents increment in liability of a long-term borrowing due to exchange rate fluctuation between acquisition date and balance sheet date.

8. What will be the classification for following items in the statement of cash flows of both (i) Banks / Financial institutions and (ii) Other Entities?

S. No.	Particulars
1	Interest received on loans and advances given
2	Interest paid on deposits and other borrowings
3	Interest and dividend received on investments in subsidiaries, associates and in

© The Institute of Chartered Accountants of India

	other entities
4	Dividend paid on preference and equity shares, including tax on dividend paid on preference and equity shares by other entities
5	Finance charges paid by lessee under finance lease
6	Payment towards reduction of outstanding finance lease liability
7	Interest paid to vendor for acquiring fixed asset under deferred payment basis
8	Principal sum payment under deferred payment basis for acquisition of fixed assets
9	Penal interest received from customers for late payments
10	Penal interest paid to suppliers for late payments
11	Interest paid on delayed tax payments
12	Interest received on tax refunds

Answers

1. A. DIRECT METHOD

Cash flows from operating activities		**20X2**
Cash received from customers	2,07,500	
Cash paid for inventory	(1,24,000)	
Cash paid for insurance	(9,000)	
Cash paid for wages	(53,000)	
Net cash flow from operating activities		21,500
Cash flows from investing activities		
Purchase of fixed assets		(46,000)
Cash flows from financing activities		
Dividend paid	(2,500)	
Proceeds from issuance of debentures	13,000	
Proceeds from issue of equity	4,000	
Net cash flows from financing activities		14,500
Net decrease in cash and cash equivalents		**(10,000)**
Opening Cash Balance		**14,000**
Closing Cash Balance		**4,000**

B. INDIRECT METHOD

Cash flows from operating activities		**20X2**
Net Profit	1,000	
Adjustments for Depreciation	15,000	

© The Institute of Chartered Accountants of India

	16,000	
Decrease in accounts receivable	7,500	
Decrease in prepaid insurance	2,000	
Increase in inventory	(3,000)	
Increase in accounts payable	2,000	
Decrease in wages payable	(3,000)	
Net cash flow from operating activities		21,500
Cash flows from investing activities		
Purchase of fixed assets		(46,000)
Cash flows from financing activities		
Dividend paid	(2,500)	
Proceeds from issue of debentures	13,000	
Proceeds from issue of equity	4,000	
Net cash flows from financing activities		14,500
Net decrease in cash and cash equivalents		**(10,000)**
Opening Cash Balance		**14,000**
Closing Cash Balance		**4,000**

Working Notes:

Fixed Assets Account

Particulars	Amount (₹)	Particulars	Amount (₹)
To Balance b/d	2,70,000	By Balance c/d	3,16,000
To Cash (Purchase of Fixed Assets)	46,000		
	3,16,000		3,16,000

Inventory Account

Particulars	Amount (₹)	Particulars	Amount (₹)
To Balance b/d	34,000	By Cost of goods sold	1,23,000
To Creditors account (credit purchase)	2,000	By Balance c/d	37,000
To Purchase (Bal. Figure)	1,24,000		
	1,60,000		**1,60,000**

© The Institute of Chartered Accountants of India

Accounts Payable Account

Particulars	Amount (₹)	Particulars	Amount (₹)
To Balance c/d	18,000	By Balance b/d	16,000
		By Inventory Account (credit purchase) (Bal.Fig.)	2,000
	18,000		**18,000**

Equity Share Capital Account

Particulars	Amount (₹)	Particulars	Amount (₹)
To Balance c/d	88,000	By Balance b/d	84,000
		By Bank account (Proceeds from equity share issued)	4,000
	88,000		**88,000**

2. **XYZ Ltd.**

Cash Flow Statement for the year ended March 31, 20X1 (Using the Direct Method)

Cash flows from operating activities	₹ '000	₹ '000
Cash receipts from customers	2,800	
Cash payments to suppliers	(2,000)	
Cash paid to employees	(100)	
Cash payments for overheads	(200)	
Cash generated from operations	500	
Income tax paid	(250)	
Net cash from operating activities		250
Cash flow from investing activities		
Payments for purchase of fixed assets	(200)	
Proceeds from sale of fixed assets	100	
Net cash used in investing activities		(100)
Cash flows from financing activities		
Proceeds from issuance of equity shares	300	
Bank loan repaid	(300)	

© The Institute of Chartered Accountants of India

Dividend paid	(50)	
Net cash used in financing activities		(50)
Net increase in cash		**100**
Cash at the beginning of the period		**50**
Cash at end of the period		**150**

3. The profit and loss account was credited by ₹ 1,00,000 (US $ 2,000 × ₹ 50) towards interest income. It was credited by the exchange difference of US$ 1,00,000 × (₹ 50 - ₹ 45) that is, ₹ 500,000. In preparing the cash flow statement, ₹ 5,00,000, the exchange difference, should be deducted from the 'net profit before taxes'. However, in order to reconcile the opening balance of the cash and cash equivalents with its closing balance, the exchange difference ₹ 5,00,000, should be added to the opening balance in note to cash flow statement.

Cash flows arising from transactions in a foreign currency shall be recorded in Z Ltd.'s functional currency by applying to the foreign currency amount the exchange rate between the functional currency and the foreign currency at the date of the cash flow.

4. As per para 39 of Ind AS 7, the aggregate cash flows arising from obtaining control of subsidiary shall be presented separately and classified as investing activities.

As per para 42 of Ind AS 7, the aggregate amount of the cash paid or received as consideration for obtaining subsidiaries is reported in the statement of cash flows net of cash and cash equivalents acquired or disposed of as part of such transactions, events or changes in circumstances.

Further, investing and financing transactions that do not require the use of cash or cash equivalents shall be excluded from a statement of cash flows. Such transactions shall be disclosed elsewhere in the financial statements in a way that provides all the relevant information about these investing and financing activities.

As per para 42A of Ind AS 7, cash flows arising from changes in ownership interests in a subsidiary that do not result in a loss of control shall be classified as cash flows from financing activities, unless the subsidiary is held by an investment entity, as defined in Ind AS 110, and is required to be measured at fair value through profit or loss. Such transactions are accounted for as equity transactions and accordingly, the resulting cash flows are classified in the same way as other transactions with owners.

Considering the above, for the financial year ended 31st March, 20X2 total consideration of ₹ 15,00,000 less ₹ 250,000 will be shown under investing activities as "Acquisition of the subsidiary (net of cash acquired)".

There will not be any impact of issuance of equity shares as consideration in the cash flow statement however a proper disclosure shall be given elsewhere in the financial statements in a way that provides all the relevant information about the issuance of equity shares for non-cash consideration.

© The Institute of Chartered Accountants of India

Further, in the statement of cash flows for the year ended 31st March, 20X3, cash consideration paid for the acquisition of additional 10% stake in Company B will be shown under financing activities.

5. This information will be incorporated into the Consolidated Statement of Cash Flows as follows:

Statement of Cash Flows for the year ended 20X2 (extract)

	Amount (₹)	Amount (₹)
Cash flows from operating activities		
Profit before taxation	70,000	
Adjustments for non-cash items:		
Depreciation	30,000	
Decrease in inventories (W.N. 1)	9,000	
Decrease in trade receivables (W.N. 2)	4,000	
Decrease in trade payables (W.N. 3)	(24,000)	
Interest paid to be included in financing activities	4,000	
Taxation (11,000 + 15,000 – 12,000)	(14,000)	
Net cash generated from operating activities		79,000
Cash flows from investing activities		
Cash paid to acquire subsidiary (74,000 – 2,000)	(72,000)	
Net cash outflow from investing activities		(72,000)
Cash flows from financing activities		
Interest paid	(4,000)	
Net cash outflow from financing activities		(4,000)
Increase in cash and cash equivalents during the year		**3,000**
Cash and cash equivalents at the beginning of the year		**5,000**
Cash and cash equivalents at the end of the year		**8,000**

Working Notes:

1.

Calculation of change in inventory during the year	₹
Total inventories of the Group at the end of the year	30,000
Inventories acquired during the year from subsidiary	(4,000)

© The Institute of Chartered Accountants of India

	26,000
Opening inventories	35,000
Decrease in inventories	9,000

2.

Calculation of change in Trade Receivables during the year	₹
Total trade receivables of the Group at the end of the year	54,000
Trade receivables acquired during the year from subsidiary	(8,000)
	46,000
Opening trade receivables	50,000
Decrease in trade receivables	4,000

3.

Calculation of change in Trade Payables during the year	₹
Trade payables at the end of the year	68,000
Trade payables of the subsidiary assumed during the year	(32,000)
	36,000
Opening trade payables	60,000
Decrease in trade payables	24,000

6. Para 36 of Ind AS 7 inter alia states that when it is practicable to identify the tax cash flow with an individual transaction that gives rise to cash flows that are classified as investing or financing activities the tax cash flow is classified as an investing or financing activity as appropriate. When tax cash flows are allocated over more than one class of activity, the total amount of taxes paid is disclosed.

   Accordingly, the transactions are analysed as follows:

Particulars	Amount (in crore)	Activity
Sale Consideration	100	Investing Activity
Capital Gain Tax	(20)	Investing Activity
Business profits	30	Operating Activity
Tax on Business profits	(3)	Operating Activity
Dividend Payment	(20)	Financing Activity
Dividend Distribution Tax	(2)	Financing Activity
Income Tax Refund	1.5	Operating Activity
Total Cash flow	**86.5**	

© The Institute of Chartered Accountants of India

Activity wise	Amount (in crore)
Operating Activity	28.5
Investing Activity	80
Financing Activity	(22)
Total	**86.5**

7. **Statement Cash Flows from operating activities of Galaxy Ltd. for the year ended 31st March 20X2 (Direct Method)**

Particulars	₹	₹
Operating Activities:		
Cash received from Trade receivables (W.N. 3)		85,33,000
Less: Cash paid to Suppliers (W.N.2)	55,75,000	
Payment for Administration and Selling expenses	15,40,000	
Payment for Income Tax (W.N.4)	1,12,000	(72,27,000)
		13,06,000
Adjustment for exceptional items (fire insurance claim)		1,10,000
Net cash generated from operating activities		14,16,000

Working Notes:

1. **Calculation of total purchases**

   Cost of Sales = Opening stock + Purchases – Closing Stock

   ₹ 56,00,000 = ₹ 1,65,000 + Purchases – ₹ 1,20,000

   Purchases = ₹ 55,55,000

2. **Calculation of cash paid to Suppliers**

Trade Payables

	₹		₹
To Bank A/c (balancing figure)	55,75,000	By Balance b/d	2,15,000
To Balance c/d	1,95,000	By Purchases (W.N. 1)	55,55,000
	57,70,000		57,70,000

© The Institute of Chartered Accountants of India

3. Calculation of cash received from Customers

Trade Receivables

	₹		₹
To Balance b/d	1,88,000	By Bank A/c (balancing figure)	85,33,000
To Sales	85,50,000	By Balance c/d	2,05,000
	87,38,000		87,38,000

4. Calculation of tax paid during the year in cash

Provision for tax

	₹		₹
To Bank A/c (balancing figure)	1,12,000	By Balance b/d	65,000
To Balance c/d	48,000	By Profit and Loss A/c	95,000
	1,60,000		1,60,000

8. The following are the classification of various activities in the Statement of Cash Flows:

S. No.	Particulars	Classification for reporting cash flows	
		Banks / financial institutions	Other entities
1	Interest received on loans and advances given	Operating Activities	Investing activities
2	Interest paid on deposits and other borrowings	Operating Activities	Financing activities
3	Interest and dividend received on investments in subsidiaries, associates and in other entities	Investing activities	Investing activities
4	Dividend paid on preference and equity shares, including tax on dividend paid on preference and equity shares by other entities	Financing activities	Financing activities
5	Finance charges paid by lessee under finance lease	Financing activities	Financing activities
6	Payment towards reduction of outstanding finance lease liability	Financing activities	Financing activities

© The Institute of Chartered Accountants of India

7	Interest paid to vendor for acquiring fixed asset under deferred payment basis	Financing activities	Financing activities
8	Principal sum payment under deferred payment basis for acquisition of fixed assets	Investing activities	Investing activities
9	Penal interest received from customers for late payments	Operating Activities	Operating Activities
10	Penal interest paid to suppliers for late payments	Operating Activities	Operating Activities
11	Interest paid on delayed tax payments	Operating Activities	Operating Activities
12	Interest received on tax refunds	Operating Activities	Operating Activities

© The Institute of Chartered Accountants of India

FOR SHORTCUT TO IND AS WISDOM: SCAN ME!

TEST YOUR KNOWLEDGE

Questions

1. A carpet retail outlet sells and fits carpets to the general public. It recognizes revenue when the carpet is fitted, which on an average is six weeks after the purchase of the carpet.

   It then decides to sub-contract the fitting of carpets to self-employed fitters. It now recognizes revenue at the point-of-sale of the carpet.

   Whether this change in recognising the revenue is a change in accounting policy as per the provision of Ind AS 8?

2. Under what circumstances an entity is required to present a third balance sheet at the beginning of the preceding period?

3. During 20X2, Delta Ltd., changed its accounting policy for depreciating property, plant and equipment, so as to apply a component approach completely, whilst at the same time adopting the revaluation model.

   In years before 20X2, Delta Ltd.'s asset records were not sufficiently detailed to apply a component approach fully. At the end of 20X1, management commissioned an engineering survey, which provided information on the components held and their fair values, useful lives, estimated residual values and depreciable amounts at the beginning of 20X2. However, the survey did not provide a sufficient basis for reliably estimating the cost of those components that had not previously been accounted for separately, and the existing records before the survey did not permit this information to be reconstructed.

   Delta Ltd.'s management considered how to account for each of the two aspects of the accounting change. They determined that it was not practicable to account for the change to a fuller component approach retrospectively, or to account for that change prospectively from any earlier date than the start of 20X2. Also, the change from a cost model to a revaluation

© The Institute of Chartered Accountants of India

model is required to be accounted for prospectively. Therefore, management concluded that it should apply Delta Ltd.'s new policy prospectively from the start of 20X2.

Additional information:

(i) Delta Ltd.'s tax rate is 30%

(ii) Property, plant and equipment at the end of 20X1:

Cost	₹ 25,000
Depreciation	₹ 14,000
Net book value	₹ 11,000

(iii) Prospective depreciation expense for 20X2 (old basis) ₹ 1,500

(iv) Some results of the engineering survey:

Valuation	₹ 17,000
Estimated residual value	₹ 3,000
Average remaining asset life	7 years
Depreciation expense on existing property, plant and equipment for 20X2 (new basis)	₹ 2,000

You are required to prepare the relevant note for disclosure in accordance with Ind AS 8.

4. Is change in the depreciation method for an item of property, plant and equipment a change in accounting policy or a change in accounting estimate?

5. An entity charged off certain expenses as finance costs in its financial statements for the year ended 31st March, 20X1. While preparing annual financial statements for the year ended 31st March, 20X2, management discovered that these expenses should have been classified as other expenses instead of finance costs. The error occurred because the management inadvertently misinterpreted certain facts. The entity intends to restate the comparative amounts for the prior period presented in which the error occurred (i.e., year ended 31st March, 20X1). Would this reclassification of expenses from finance costs to other expenses in the comparative amounts will be considered as correction of an error under Ind AS 8? Would the entity need to present a third balance sheet?

6. While preparing the annual financial statements for the year ended 31st March, 20X3, an entity discovers that a provision for constructive obligation for payment of bonus to selected employees in corporate office (material in amount) which was required to be recognised in the annual financial statements for the year ended 31st March, 20X1 was not recognised due to oversight of facts. The bonus was paid during the financial year ended 31st March, 20X2 and was recognised as an expense in the annual financial statements for

© The Institute of Chartered Accountants of India

the said year. Would this situation require retrospective restatement of comparatives considering that the amount was material?

7. While preparing interim financial statements for the half-year ended 30th September, 20X1, an entity notes that there has been an under-accrual of certain expenses in the interim financial statements for the first quarter ended 30th June, 20X1. The amount of under accrual is assessed to be material in the context of interim financial statements. However, it is expected that the amount would be immaterial in the context of the annual financial statements. The management is of the view that there is no need to correct the error in the interim financial statements considering that the amount is expected to be immaterial from the point of view of the annual financial statements. Whether the management's view is acceptable?

8. ABC Ltd has an investment property with an original cost of ₹ 1,00,000 which it inadvertently omitted to depreciate in previous financial statements. The property was acquired on 1st April, 20X1. The property has a useful life of 10 years and is depreciated using straight line method. Estimated residual value at the end of 10 year is Nil.

   How should the error be corrected in the financial statements for the year ended 31st March, 20X4, assuming the impact of the same is considered material? For simplicity, ignore tax effects.

9. ABC Ltd. changed its method adopted for inventory valuation in the year 20X2-20X3. Prior to the change, inventory was valued using the first in first out method (FIFO). However, it was felt that in order to match current practice and to make the financial statements more relevant and reliable, a weighted average valuation model would be more appropriate.

   The effect of the change in the method of valuation of inventory was as follows:

   - 31st March, 20X1 - Increase of ₹ 10 million
   - 31st March, 20X2 - Increase of ₹ 15 million
   - 31st March, 20X3 - Increase of ₹ 20 million

   Profit or loss under the FIFO valuation model are as follows:

	20X2-20X3	20X1-20X2
Revenue	324	296
Cost of goods sold	(173)	(164)
Gross profit	**151**	**132**
Expenses	(83)	(74)
Profit	**68**	**58**

   Retained earnings at 31st March, 20X1 were ₹ 423 million

© The Institute of Chartered Accountants of India

You are required to present the impact of change in accounting policy in the profit or loss and produce an extract of the statement of changes in equity in accordance with Ind AS 8.

10. During 20X4-20X5, Cheery Limited discovered that some products that had been sold during 20X3-20X4 were incorrectly included in inventory at 31st March, 20X4 at ₹ 6,500.

    Cheery Limited's accounting records for 20X4-20X5 show sales of ₹ 104,000, cost of goods sold of ₹ 86,500 (including ₹ 6,500 for the error in opening inventory), and income taxes of ₹ 5,250.

    In 20X3-20X4, Cheery Limited reported:

	₹
Sales	73,500
Cost of goods sold	(53,500)
Profit before income taxes	20,000
Income taxes	(6,000)
Profit	14,000
Basic and diluted EPS	2.8

    The 20X3-20X4 opening retained earnings was ₹ 20,000 and closing retained earnings was ₹ 34,000. Cheery Limited's income tax rate was 30% for 20X4-20X5 and 20X3-20X4. It had no other income or expenses.

    Cheery Limited had ₹ 50,000 (5,000 shares of ₹ 10 each) of share capital throughout, and no other components of equity except for retained earnings.

    State how the above will be treated /accounted in Cheery Limited's Statement of profit and loss, statement of changes in equity and in notes wherever required for current period and earlier period(s) as per relevant Ind AS.

11. In 20X3-20X4, after the entity's 31st March 20X3 annual financial statements were approved for issue, a latent defect in the composition of a new product manufactured by the entity was discovered (that is, a defect that could not be discovered by reasonable or customary inspection). As a result of the latent defect the entity incurred ₹ 1,00,000 of unanticipated costs for fulfilling its warranty obligation in respect of sales made before 31st March 20X3. An additional ₹ 20,000 was incurred to rectify the latent defect in products sold during 20X3-20X4 before the defect was detected and the production process rectified, ₹ 5,000 of which relates to items of inventory at 31st March 20X3. The defective inventory was reported at cost ₹ 15,000 in the 20X2-20X3 financial statements when its selling price less costs to complete and sell was estimated at ₹ 18,000. The accounting estimates made in preparing the 31st March 20X3 financial statements were appropriately made using all reliable information that the entity could reasonably be expected to have been obtained and taken into account in the preparation and presentation of those financial statements.

    Analyse the above situation in accordance with relevant Ind AS.

© The Institute of Chartered Accountants of India

Answers

1. This is not a change in accounting policy as the carpet retailer has changed the way that the carpets are fitted.

   Therefore, there would not be any need to retrospectively change the prior period figures for revenue already recognized.

2. As per paragraph 40A of Ind AS 1, Presentation of Financial Statements, an entity shall present a third balance sheet as at the beginning of the preceding period in addition to the minimum comparative financial statements required by paragraph 38A of the standard if:

   - it applies an accounting policy retrospectively, makes a retrospective restatement of items in its financial statements or reclassifies items in its financial statements; and
   - the retrospective application, retrospective restatement or the reclassification has a material effect on the information in the balance sheet at the beginning of the preceding period.

3. **Extract from the notes**

   From the start of 20X2, Delta Ltd., changed its accounting policy for depreciating property, plant and equipment, so as to apply much more fully a components approach, whilst at the same time adopting the revaluation model. Management takes the view that this policy provides reliable and more relevant information because it deals more accurately with the components of property, plant and equipment and is based on up-to-date values. The policy has been applied prospectively from the start of 20X2 because it was not practicable to estimate the effects of applying the policy either retrospectively, or prospectively from any earlier date. Accordingly, the adoption of the new policy has no effect on prior years. The effect on the current year is to increase the carrying amount of property, plant and equipment at the start of the year by ₹ 6,000; increase the opening deferred tax provision by ₹ 1,800; create a revaluation surplus at the start of the year of ₹ 4,200; increase depreciation expense by ₹ 500; and reduce tax expense by ₹ 150.

4. As per paragraphs 60 and 61 of Ind AS 16, Property, Plant and Equipment, the depreciation method used shall reflect the pattern in which the asset's future economic benefits are expected to be consumed by the entity. The depreciation method applied to an asset shall be reviewed at least at each financial year-end and, if there has been a significant change in the expected pattern of consumption of the future economic benefits embodied in the asset, the method shall be changed to reflect the changed pattern. Such a change is accounted for as a change in an accounting estimate in accordance with Ind AS 8.

   As per the above, depreciation method for a depreciable asset has to reflect the expected pattern of consumption of future economic benefits embodied in the asset. Determination

© The Institute of Chartered Accountants of India

of depreciation method involves an accounting estimate and thus depreciation method is not a matter of an accounting policy.

Accordingly, Ind AS 16 requires a change in depreciation method to be accounted for as a change in an accounting estimate, i.e., prospectively.

5. As per paragraph 41 of Ind AS 8, errors can arise in respect of the recognition, measurement, presentation or disclosure of elements of financial statements. Financial statements do not comply with Ind AS if they contain either material errors or immaterial errors made intentionally to achieve a particular presentation of an entity's financial position, financial performance or cash flows. Potential current period errors discovered in that period are corrected before the financial statements are approved for issue. However, material errors are sometimes not discovered until a subsequent period, and these prior period errors are corrected in the comparative information presented in the financial statements for that subsequent period.

In accordance with the above, the reclassification of expenses from finance costs to other expenses would be considered as correction of an error under Ind AS 8. Accordingly, in the financial statements for the year ended 31st March, 20X2, the comparative amounts for the year ended 31st March, 20X1 would be restated to reflect the correct classification.

Ind AS 1 requires an entity to present a third balance sheet as at the beginning of the preceding period in addition to the minimum comparative financial statements if, inter alia, it makes a retrospective restatement of items in its financial statements and the restatement has a material effect on the information in the balance sheet at the beginning of the preceding period.

In the given case, the retrospective restatement of relevant items in statement of profit and loss has no effect on the information in the balance sheet at the beginning of the preceding period (1st April, 20X0). Therefore, the entity is not required to present a third balance sheet.

6. As per paragraph 41 of Ind AS 8, errors can arise in respect of the recognition, measurement, presentation or disclosure of elements of financial statements. Financial statements do not comply with Ind AS if they contain either material errors or immaterial errors made intentionally to achieve a particular presentation of an entity's financial position, financial performance or cash flows. Potential current period errors discovered in that period are corrected before the financial statements are approved for issue. However, material errors are sometimes not discovered until a subsequent period, and these prior period errors are corrected in the comparative information presented in the financial statements for that subsequent period.

As per paragraph 40A of Ind AS 1, an entity shall present a third balance sheet as at the beginning of the preceding period in addition to the minimum comparative financial statements if, inter alia, it makes a retrospective restatement of items in its financial

© The Institute of Chartered Accountants of India

statements and the retrospective restatement has a material effect on the information in the balance sheet at the beginning of the preceding period.

In the given case, expenses for the year ended 31st March, 20X1 and liabilities as at 31st March, 20X1 were understated because of non-recognition of bonus expense and related provision. Expenses for the year ended 31st March, 20X2, on the other hand, were overstated to the same extent because of recognition of the aforesaid bonus as expense for the year. To correct the above errors in the annual financial statements for the year ended 31st March, 20X3, the entity should:

(a) restate the comparative amounts (i.e., those for the year ended 31st March, 20X2) in the statement of profit and loss; and

(b) present a third balance sheet as at the beginning of the preceding period (i.e., as at 1st April, 20X1) wherein it should recognise the provision for bonus and restate the retained earnings.

7. Paragraph 41 of Ind AS 8, inter alia, states that financial statements do not comply with Ind AS if they contain either material errors or immaterial errors made intentionally to achieve a particular presentation of an entity's financial position, financial performance or cash flows.

As regards the assessment of materiality of an item in preparing interim financial statements, paragraph 25 of Ind AS 34, Interim Financial Statements, states as follows:

"While judgement is always required in assessing materiality, this Standard bases the recognition and disclosure decision on data for the interim period by itself for reasons of understandability of the interim figures. Thus, for example, unusual items, changes in accounting policies or estimates, and errors are recognised and disclosed on the basis of materiality in relation to interim period data to avoid misleading inferences that might result from non-disclosure. The overriding goal is to ensure that an interim financial report includes all information that is relevant to understanding of an entity's financial position and performance during the interim period."

As per the above, while materiality judgements always involve a degree of subjectivity, the overriding goal is to ensure that an interim financial report includes all the information that is relevant to an understanding of the financial position and performance of the entity during the interim period. It is therefore not appropriate to base quantitative assessments of materiality on projected annual figures when evaluating errors in interim financial statements.

Accordingly, the management is required to correct the error in the interim financial statements since it is assessed to be material in relation to interim period data.

© The Institute of Chartered Accountants of India

8. The error shall be corrected by retrospectively restating the figures for financial year 20X2-20X3 and also by presenting a third balance sheet as at 1st April, 20X2 which is the beginning of the earliest period presented in the financial statements.

9. **Profit or loss under weighted average valuation method is as follows:**

	20X2-20X3	20X1-20X2 (Restated)
Revenue	324	296
Cost of goods sold	(168)	(159)
Gross profit	**156**	**137**
Expenses	(83)	(74)
Profit	**73**	**63**

Statement of changes in Equity (extract)

	Retained earnings	Retained earnings (Original)
At 1st April, 20X1	423	423
Change in inventory valuation policy	10	-
At 1st April, 20X1 (Restated)	**433**	**-**
Profit for the year 20X1-20X2	63	58
At 31st March, 20X2	**496**	**481**
Profit for the 20X2-20X3	73	68
At 31st March, 20X3	**569**	**549**

10. **Cheery Limited**

Extract from the Statement of profit and loss

	20X4-20X5 ₹	(Restated) 20X3-20X4 ₹
Sales	1,04,000	73,500
Cost of goods sold	(80,000)	(60,000)
Profit before income taxes	**24,000**	**13,500**
Income taxes	(7,200)	(4,050)
Profit	**16,800**	**9,450**
Basic and diluted EPS	3.36	1.89

© The Institute of Chartered Accountants of India

Cheery Limited
Statement of Changes in Equity

	Share capital	Retained earnings	Total
Balance at 31st March, 20X3	50,000	20,000	70,000
Profit for the year ended 31st March, 20X4 as restated	____	9,450	9,450
Balance at 31st March, 20X4	**50,000**	**29,450**	**79,450**
Profit for the year ended 31st March, 20X5	____	16,800	16,800
Balance at 31st March, 20X5	**50,000**	**46,250**	**96,250**

Extract from the Notes

Some products that had been sold in 20X3-20X4 were incorrectly included in inventory at 31st March, 20X4 at ₹ 6,500. The financial statements of 20X3-20X4 have been restated to correct this error. The effect of the restatement on those financial statements is summarized below:

	Effect on 20X3-20X4
(Increase) in cost of goods sold	(6,500)
Decrease in income tax expenses	1,950
(Decrease) in profit	(4,550)
(Decrease) in basic and diluted EPS	(0.91)
(Decrease) in inventory	(6,500)
Decrease in income tax payable	1,950
(Decrease) in equity	(4,550)

There is no effect on the balance sheet at the beginning of the preceding period i.e. 1st April, 20X3.

11. Ind AS 8 is applied in selecting and applying accounting policies, and accounting for changes in accounting policies, changes in accounting estimates and corrections of prior period errors.

A change in accounting estimate is an adjustment of the carrying amount of an asset or a liability, or the amount of the periodic consumption of an asset. This change in accounting estimate is an outcome of the assessment of the present status of, and expected future benefits and obligations associated with, assets and liabilities. Changes in accounting

© The Institute of Chartered Accountants of India

estimates result from new information or new developments and, accordingly, are not corrections of errors.

Further, the effect of change in an accounting estimate, shall be recognised prospectively by including it in profit or loss in: (a) the period of the change, if the change affects that period only; or (b) the period of the change and future periods, if the change affects both.

Prior period errors are omissions from, and misstatements in, the entity's financial statements for one or more prior periods arising from a failure to use, or misuse of, reliable information that:

(a) was available when financial statements for those periods were approved for issue; and

(b) could reasonably be expected to have been obtained and taken into account in the preparation and presentation of those financial statements.

Such errors include the effects of mathematical mistakes, mistakes in applying accounting policies, oversights or misinterpretations of facts, and fraud.

On the basis of above provisions, the given situation would be dealt as follows:

The defect was neither known nor reasonably possible to detect at 31st March 20X3 or before the financial statements were approved for issue, so understatement of the warranty provision ₹ 1,00,000 and overstatement of inventory ₹ 2,000 (Note 1) in the 31st March 20X3 financial statements are not prior period errors.

The effects of the latent defect that relate to the entity's financial position at 31st March 20X3 are changes in accounting estimates.

In preparing its financial statements for 31st March 20X3, the entity made the warranty provision and inventory valuation appropriately using all reliable information that the entity could reasonably be expected to have obtained and had taken into account the same in the preparation and presentation of those financial statements.

Consequently, the additional costs are expensed in calculating profit or loss for 20X3-20X4.

Working Note:

Inventory is measured at the lower of cost (i.e. ₹ 15,000) and fair value less costs to complete and sell (i.e. ₹ 18,000 originally estimated minus ₹ 5,000 costs to rectify latent defect) = ₹ 13,000.

© The Institute of Chartered Accountants of India

FOR SHORTCUT TO IND AS WISDOM: SCAN ME!

TEST YOUR KNOWLEDGE

Questions

1. The AGM of ABC Ltd for the year ended 31st March, 20X2 was held on 10th July, 20X2 and Board Meeting has been conducted on 15th May, 20X2. Meanwhile, the company had to disclose certain financial information pertaining to the year ended 31st March, 20X2 to SEBI as per SEBI regulations on 20th April, 20X2. Since, certain financial information pertaining to the year ended 31st March, 20X2 is submitted to SEBI before approval of financial statements by the Board, the management is suggesting that 20th April 20X2 shall be considered as 'after the reporting period'. Whether the management view is correct in accordance with the guidance given in Ind AS 10?

2. ABC Ltd. is in a legal suit against the GST department. The company gets a court order in its favour on 15th April, 20X2, which resulted into reducing the tax liability as on 31st March, 20X2. The financial statements for 20X1-20X2 were approved by the board of directors on 15th May, 20X2. The management has not considered the effect of the transaction as the event is favourable to the company. The company's view is that favourable events after the reporting period should not be considered as it would hamper the realisation concept of accounting. Comment on the company's views in the light of Ind AS 10.

3. ABC Ltd. trades in laptops. On 31st March, 20X2, the company has 50 laptops which were purchased at ₹ 45,000 each. The company has considered the same price for calculation of closing inventory valuation. On 15th April, 20X2, advanced version of same series of laptops is introduced in the market. Therefore, the price of the current laptops goes down to ₹ 35,000 each. The financial statements for 20X1-20X2 were approved by the board of directors on 15th May, 20X2. The company does not want to value the stock at ₹ 35,000

© The Institute of Chartered Accountants of India

less estimated costs necessary to make the sale as the event of reduction in selling price took place after 31st March, 20X2 and the reduced prices were not applicable as on 31st March, 20X2. Comment on the company's views.

4. XY Ltd took a large-sized civil construction contract, for a public sector undertaking, valued at ₹ 200 crores. The execution of the project started during 20X1-20X2 and continued in the next financial year also. During execution of the work on 29th May, 20X2, the company found while raising the foundation work that it had met a rocky surface and cost of contract would go up by an extra ₹ 50 crores, which would not be recoverable from the contractee as per the terms of the contract. The Company's financial year ended on 31st March, 20X2, and the financial statements were considered and approved by the Board of Directors on 15th June, 20X2. How will you treat the above in the financial statements for the year ended 31st March, 20X2?

5. A Ltd. was required to pay a penalty for a breach in the performance of a contract. A Ltd. believed that the penalty was payable at a lower amount than the amount demanded by the other party. A Ltd. created provision for the penalty but also approached the arbitrator with a submission that the case may be dismissed with costs. A Ltd. prepared the financial statements for the year 20X1-20X2, which were approved in May, 20X2. The arbitrator, in April, 20X2, awarded the case in favour of A Ltd. As a result of the award of the arbitrator, the provision earlier made by A Ltd. was required to be reduced. The arbitrator also decided that cost of the case should be borne by the other party. Now, whether A Ltd. is required to remeasure its provision and what would be the accounting treatment of the cost that will be recovered by A Ltd., which has already been charged to the Statement of Profit and Loss as an expense for the year 20X1-20X2?

6. A company manufacturing and supplying process control equipment is entitled to duty drawback if it exceeds its turnover above a specified limit. To claim duty drawback, the company needs to file an application within 15 days of meeting the specified turnover. If the application is not filed within stipulated time, the Department has discretionary power of giving duty draw back credit. For the year 20X1-20X2, the company has exceeded the specified limit of turnover by the end of the reporting period but the application for duty drawback is filed on 20th April, 20X2, which is after the stipulated time of 15 days of meeting the turnover condition.

   Duty drawback has been credited by the Department on 28th June, 20X2 and financial statements have been approved by the Board of Directors of the company on 26th July, 20X2. Whether duty drawback credit should be treated as an adjusting event?

7. XYZ Ltd. sells goods to its customer with a promise to give a discount of 5% on list price of the goods provided that the payments are received from customer within 15 days. XYZ Ltd.

© The Institute of Chartered Accountants of India

sold goods for ₹ 5 lakhs to ABC Ltd. between 17th March, 20X2 and 31st March, 20X2. ABC Ltd. paid the dues by 15th April, 20X2 with respect to sales made between 17th March, 20X2 and 31st March, 20X2. Financial statements were approved for issue by Board of Directors on 31st May, 20X2.

State whether discount will be adjusted from the sales at the end of the reporting period.

8. Whether the fraud related to 20X1-20X2 discovered after the end of the reporting period but before the date of approval of financial statements for 20X3-20X4 is an adjusting event?

9. X Ltd. was having investment in the form of equity shares in another company as at the end of the reporting period, i.e., 31st March, 20X2. After the end of the reporting period but before the approval of the financial statements it has been found that value of investment was fraudulently inflated by committing a computation error. Whether such event should be adjusted in the financial statements for the year 20X1-20X2?

10. ABC Ltd. received a demand notice on 15th June, 20X2 for an additional amount of ₹ 28,00,000 from the Excise Department on account of higher excise duty levied by the Excise Department compared to the rate at which the company was creating provision and depositing the same in respect of transactions related to financial year 20X1-20X2. The financial statements for the year 20X1-20X2 are approved on 10th August, 20X2. In July, 20X2, the company has appealed against the demand of ₹ 28,00,000 and the company has expected that the demand would be settled at ₹ 15,00,000 only. Show how the above event will have a bearing on the financial statements for the year 20X1-20X2. Whether these events are adjusting or non-adjusting events and explain the treatment accordingly.

Answers

1. As per Ind AS 10, even if partial information has already been published, the reporting period will be considered as the period between the end of the reporting period and the date of approval of financial statements. In the above case, the financial statements for the year 20X1-20X2 were approved on 15th May, 20X2. Therefore, for the purposes of Ind AS 10, 'after the reporting period' would be the period between 31st March, 20X2 and 15th May, 20X2.

2. As per Ind AS 10, even favourable events need to be considered. What is important is whether a condition exists as at the end of the reporting period and there is evidence for the same.

3. As per Ind AS 10, the decrease in the net realizable value of the stock after the reporting period should normally be considered as an adjusting event.

© The Institute of Chartered Accountants of India

4. In the instant case, the execution of work started during the financial year 20X1-20X2 and the rocky surface was there at the end of the reporting period, though the existence of rocky surface is confirmed after the end of the reporting period as a result of which it became evident that the cost may escalate by ₹ 50 crores. In accordance with the definition of 'Events after the Reporting Period', since the rocky surface was there, the condition was existing at the end of the reporting period, therefore, it is an adjusting event. The cost of the project and profit should be accounted for accordingly.

5. In the instant case, A Ltd. approached the arbitrator before the end of the reporting period, who decided the award after the end of the reporting period but before approval of the financial statements for issue. Accordingly, the conditions were existing at the end of the reporting date because A Ltd. had approached the arbitrator before the end of the reporting period whose outcome has been confirmed by the award of the arbitrator. Therefore, it is an adjusting event.

Accordingly, the measurement of the provision is required to be adjusted for the event occurring after the reporting period. As far as the recovery of the cost by A Ltd. from the other party is concerned, this right to recover was a contingent asset as at the end of the reporting period.

As per para 35 of Ind AS 37, contingent assets are assessed continually to ensure that developments are appropriately reflected in the financial statements. If it has become virtually certain that an inflow of economic benefits will arise, the asset and the related income are recognised in the financial statements of the period in which the change occurs. If an inflow of economic benefits has become probable, an entity discloses the contingent asset.

On the basis of the above, a contingent asset should be recognised in the financial statements of the period in which the realisation of asset and the related income becomes virtually certain. In the instant case, the recovery of cost became certain when the arbitrator decided the award during financial year 20X2-20X3.

Accordingly, the recovery of cost should be recognised in the financial year 20X2-20X3.

6. In the instant case, the condition of exceeding the specified turnover was met at the end of the reporting period and the company was entitled to the duty draw back but the application for the same has been filed after the stipulated time. Therefore, credit of duty drawback is discretionary in the hands of the Department. Accordingly, the duty drawback credit is a contingent asset as at the end of the reporting period, which may be realized if the Department credits the same.

© The Institute of Chartered Accountants of India

As per para 35 of Ind AS 37, contingent assets are assessed continually to ensure that developments are appropriately reflected in the financial statements. If it has become virtually certain that an inflow of economic benefits will arise, asset and the related income are recognized in the financial statements of the period in which the change occurs. If an inflow of economic benefits has become probable, an entity discloses the contingent asset.

In accordance with the above, the duty draw-back credit which was contingent asset for the financial year 20X1-20X2 should be recognized as asset and related income should be recognized in the reporting period in which the change occurs. i.e., in the period in which realization becomes virtually certain, i.e., financial year 20X2-20X3.

7. As per Ind AS 115, if the consideration promised in a contract includes a variable amount, an entity shall estimate the amount of consideration to which the entity will be entitled in exchange for transferring the promised goods or services to a customer.

In the instant case, the condition that sales have been made exists at the end of the reporting period and the receipt of payment within 15 days time after the end of the reporting period and before the approval of the financial statements confirms that the discount is to be provided on those sales. Therefore, it is an adjusting event. Accordingly, XYZ Ltd. should adjust the sales made to ABC Ltd. with respect to discount of 5% on the list price of the goods.

8. In the instant case, the fraud is discovered after the end of the reporting period of 20X3-20X4, which related to financial year 20X1-20X2. Since the fraud took place before the end of the reporting period, the condition was existing which has been confirmed by the detection of the same after the end of the reporting period but before the approval of financial statements. Therefore, it is an adjusting event.

Moreover, Ind AS 10 in paragraph 9, specifically provides that the discovery of fraud or error after the end of the reporting period, that shows that financial statements are incorrect, is an adjusting event. Such a discovery of fraud should be accounted for in accordance with Ind AS 8 if it meets the definition of prior period error.

9. Since it has been detected that a fraud has been made by committing an intentional error and as a result of the same financial statements present an incorrect picture, which has been detected after the end of the reporting period but before the approval of the financial statements. The same is an adjusting event. Accordingly, the value of investments in the financial statements should be adjusted for the fraudulent error in computation of value of investments.

10. Ind AS 10 defines 'Events after the Reporting Period' as follows:

Events after the reporting period are those events, favourable and unfavourable, that occur

© The Institute of Chartered Accountants of India

between the end of the reporting period and the date when the financial statements are approved by the Board of Directors in case of a company, and, by the corresponding approving authority in case of any other entity for issue. Two types of events can be identified:

(a) those that provide evidence of conditions that existed at the end of the reporting period (adjusting events after the reporting period); and

(b) those that are indicative of conditions that arose after the reporting period (non-adjusting events after the reporting period)

In the instant case, the demand notice has been received on 15th June, 20X2, which is between the end of the reporting period and the date of approval of financial statements. Therefore, it is an event after the reporting period. This demand for an additional amount has been raised because of higher rate of excise duty levied by the Excise Department in respect of goods already manufactured during the reporting period. Accordingly, the condition exists on 31st March, 20X2, as the goods have been manufactured during the reporting period on which additional excise duty has been levied and this event has been confirmed by the receipt of demand notice. Therefore, it is an adjusting event.

In accordance with the principles of Ind AS 37, the company should make a provision in the financial statements for the year 20X1-20X2, at best estimate of the expenditure to be incurred, i.e., ₹ 15,00,000.

© The Institute of Chartered Accountants of India

FOR SHORTCUT TO IND AS WISDOM: SCAN ME!

TEST YOUR KNOWLEDGE

Questions

1. An asset is sold in 2 different active markets at different prices. An entity enters into transactions in both markets and can access the price in those markets for the asset at the measurement date.

   In Market A:

   The price that would be received is ₹ 26, transaction costs in that market are ₹ 3 and the costs to transport the asset to that market are ₹ 2.

   In Market B:

   The price that would be received is ₹ 25, transaction costs in that market are ₹ 1 and the costs to transport the asset to that market are ₹ 2.

   You are required to calculate:

   (i) The fair value of the asset, if market A is the principal market, and

   (ii) The fair value of the asset, if none of the markets is principal market.

2. Company J acquires land in a business combination. The land is currently developed for industrial use as a factory site. Although the land's current use is presumed to be its highest and best use unless market or other factors suggest a different use, Company J considers the fact that nearby sites have recently been developed for residential use as high-rise apartment buildings.

   On the basis of that development and recent zoning and other changes to facilitate that development, Company J determines that the land currently used as a factory site could be developed as a residential site (e.g., for high-rise apartment buildings) and that market

© The Institute of Chartered Accountants of India

participants would take into account the potential to develop the site for residential use when pricing the land.

Determine the highest and best use of the land.

3. ABC Ltd. acquired 5% equity shares of XYZ Ltd. for ₹ 10 crores in the year 20X1-20X2. The company is in process of preparing the financial statements for the year 20X2-20X3 and is assessing the fair value at subsequent measurement of the investment made in XYZ Ltd. Based on the observable input, ABC Ltd. identified a similar nature of transaction in which PQR Ltd. acquired 20% equity shares in XYZ Ltd. for ₹ 60 crores. The price of such transaction was determined on the basis of Comparable Companies Method (CCM)- Enterprise Value (EV) / EBITDA which was 8. For the current year, the EBITDA of XYZ Ltd. is ₹ 40 crores. At the time of acquisition, the valuation was determined after considering 5% of liquidity discount and 5% of non-controlling stake discount. What will be the fair value of ABC Ltd.'s investment in XYZ Ltd. as on the balance sheet date?

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

(₹ in crores)

Particulars	Year 1	Year 2	Year 3	Year 4	Year 5
Cash flows	187.1	187.6	121.8	269	278.8
Terminal Value					3,965

The weightage average cost of capital of PT Ltd. is 11%. The total debt as on measurement date is ₹ 1,465 crores and the surplus cash & cash equivalent is ₹ 106.14 crores.

The total numbers of shares of PT Ltd. as on the measurement date is 8,52,84,223 shares. Determine value per share of PT Ltd. as per Income Approach.

5. You are a senior consultant of your firm and are in process of determining the valuation of KK Ltd. You have determined the valuation of the company by two approaches i.e. Market Approach and Income approach and selected the highest as the final value. However, based upon the discussion with your partner you have been requested to assign equal weights to both the approaches and determine a fair value of shares of KK Ltd. The details of the KK Ltd. are as follows:

Particulars	₹ in crore
Valuation as per Market Approach	5268.2
Valuation as per Income Approach	3235.2
Debt obligation as on Measurement date	1465.9

© The Institute of Chartered Accountants of India

Surplus cash & cash equivalent	106.14
Fair value of surplus assets and Liabilities	312.4
Number of shares of KK Ltd.	8,52,84,223 shares

Determine the Equity value of KK Ltd. as on the measurement date on the basis of above details.

6. Comment on the following by quoting references from appropriate Ind AS.

   (i) DS Limited holds some vacant land for which the use is not yet determined. The land is situated in a prominent area of the city where lot of commercial complexes are coming up and there is no legal restriction to convert the land into a commercial land.

   The company is not interested in developing the land to a commercial complex as it is not its business objective. Currently the land has been let out as a parking lot for the commercial complexes around.

   The Company has classified the above property as investment property. It has approached you, an expert in valuation, to obtain fair value of the land for the purpose of disclosure under Ind AS.

   On what basis will the land be fair valued under Ind AS?

   (ii) DS Limited holds equity shares of a private company. In order to determine the fair value' of the shares, the company used discounted cash flow method as there were no similar shares available in the market.

   Under which level of fair value hierarchy will the above inputs be classified?

   What will be your answer if the quoted price of similar companies were available and can be used for fair valuation of the shares?

7. On 1st January, 20X1, A Ltd assumes a decommissioning liability in a business combination. The reporting entity is legally required to dismantle and remove an offshore oil platform at the end of its useful life, which is estimated to be 10 years. The following information is relevant:

   If A Ltd was contractually allowed to transfer its decommissioning liability to a market participant, it concludes that a market participant would use all of the following inputs, probability weighted as appropriate, when estimating the price it would expect to receive:

   a. Labour costs

   Labour costs are developed based on current marketplace wages, adjusted for expectations of future wage increases, required to hire contractors to dismantle and remove offshore oil platforms. A Ltd. assigns probability to a range of cash flow estimates as follows:

© The Institute of Chartered Accountants of India

Cash Flow Estimates:	100 Cr	125 Cr	175 Cr
Probability:	25%	50%	25%

b. Allocation of overhead costs:

Assigned at 80% of labour cost

c. The compensation that a market participant would require for undertaking the activity and for assuming the risk associated with the obligation to dismantle and remove the asset. Such compensation includes both of the following:

i. Profit on labour and overhead costs:

A profit mark-up of 20% is consistent with the rate that a market participant would require as compensation for undertaking the activity

ii. The risk that the actual cash outflows might differ from those expected, excluding inflation:

A Ltd. estimates the amount of that premium to be 5% of the expected cash flows. The expected cash flows are 'real cash flows' / 'cash flows in terms of monetary value today'.

d. Effect of inflation on estimated costs and profits

A Ltd. assumes a rate of inflation of 4 percent over the 10-year period based on available market data.

e. Time value of money, represented by the risk-free rate: 5%

f. Non-performance risk relating to the risk that Entity A will not fulfill the obligation, including A Ltd.'s own credit risk: 3.5%

A Ltd, concludes that its assumptions would be used by market participants. In addition, A Ltd. does not adjust its fair value measurement for the existence of a restriction preventing it from transferring the liability.

You are required to calculate the fair value of the asset retirement obligation.

8. (i) Entity A owns 250 ordinary shares in company XYZ, an unquoted company. Company XYZ has a total share capital of 5,000 shares with nominal value of ₹ 10. Entity XYZ's after-tax maintainable profits are estimated at ₹ 70,000 per year. An appropriate price/earnings ratio determined from published industry data is 15 (before lack of marketability adjustment). Entity A's management estimates that the discount for the lack of marketability of company XYZ's shares and restrictions on their transfer is 20%. Entity A values its holding in company XYZ's shares based on earnings. Determine the fair value of Entity A's investment in XYZ's shares.

© The Institute of Chartered Accountants of India

(ii) Based on the facts given in the aforementioned part (i), assume that, Entity A estimates the fair value of the shares it owns in company XYZ using a net asset valuation technique. The fair value of company XYZ's net assets including those recognised in its balance sheet and those that are not recognised is ₹ 8,50,000. Determine the fair value of Entity A's investment in XYZ's shares.

Answers

1. (i) If Market A is the principal market

If Market A is the principal market for the asset (i.e., the market with the greatest volume and level of activity for the asset), the fair value of the asset would be measured using the price that would be received in that market, after taking into account transport costs.

Fair Value will be

	₹
Price receivable	26
Less: Transportation cost	(2)
Fair value of the asset	24

(ii) If neither of the market is the principal market

If neither of the market is the principal market for the asset, the fair value of the asset would be measured using the price in the most advantageous market. The most advantageous market is the market that maximises the amount that would be received to sell the asset, after taking into account transaction costs and transport costs (i.e., the net amount that would be received in the respective markets).

	₹	₹
	Market A	**Market B**
Price receivable	26	25
Less: Transaction cost	(3)	(1)
Less: Transportation cost	(2)	(2)
Fair value of the asset	21	22

Since the entity would maximise the net amount that would be received for the asset in Market B i.e. ₹ 22, the fair value of the asset would be measured using the price in Market B.

© The Institute of Chartered Accountants of India

Fair value

	₹
Price receivable	25
Less: Transportation cost	(2)
Fair value of the asset	23

2. The highest and best use of the land is determined by comparing the following:

   - The value of the land as currently developed for industrial use (i.e., an assumption that the land would be used in combination with other assets, such as the factory, or with other assets and liabilities); and

   - The value of the land as a vacant site for residential use, taking into account the costs of demolishing the factory and other costs necessary to convert the land to a vacant site. The value under this use would take into account risks and uncertainties about whether the entity would be able to convert the asset to the alternative use (i.e., an assumption that the land would be used by market participants on a stand-alone basis).

   The highest and best use of the land would be determined on the basis of the higher of these values. In situations involving real estate appraisal, the determination of highest and best use might take into account factors relating to the factory operations (e.g., the factory's operating cash flows) and its assets and liabilities (e.g., the factory's working capital).

3. **Determination of Enterprise Value of XYZ Ltd.**

Particulars	**₹ in crore**
EBITDA as on the measurement date	40
EV/EBITDA multiple as on the date of valuation	8
Enterprise value of XYZ Ltd.	320

Determination of subsequent measurement of XYZ Ltd.

Particulars	**₹ in crore**
Enterprise Value of XYZ Ltd.	320
ABC Ltd.'s share based on percentage of holding (5% of 320)	16
Less: Liquidity discount & Non-controlling stake discount (5%+5%=10%)	(1.6)
Fair value of ABC Ltd.'s investment in XYZ Ltd.	14.4

© The Institute of Chartered Accountants of India

4. Determination of equity value of PT Ltd.

(₹ in crore)

Particulars	Year 1	Year 2	Year 3	Year 4	Year 5
Cash flows	187.1	187.6	121.8	269	278.8
Terminal Value					3,965
Discount rate factor	0.9009	0.8116	0.7312	0.6587	0.5935
Free Cash Flow available to the firm	168.56	152.26	89.06	177.19	2,518.69
Total of all years					3,105.76
Less: Debt					(1,465)
Add: Cash & Cash equivalent					106.14
Equity Value of PT Ltd.					1,746.90
No. of Shares					85,284,223.0
Per Share Value					204.83

5. Equity Valuation of KK Ltd.

Particulars	Weights	(₹ in crore)
As per Market Approach	50	5268.2
As per Income Approach	50	3235.2
Enterprise Valuation based on weights (5268.2 x 50%) + (3235.2 x 50%)		4,251.7
Less: Debt obligation as on measurement date		(1465.9)
Add: Surplus cash & cash equivalent		106.14
Add: Fair value of surplus assets and liabilities		312.40
Enterprise value of KK Ltd.		3204.33
No. of shares		85,284,223
Value per share		375.72

6. (i) As per Ind AS 113, a fair value measurement of a non-financial asset takes into account a market participant's ability to generate economic benefits by using the asset in its highest and best use or by selling it to another market participant that would use the asset in its highest and best use.

© The Institute of Chartered Accountants of India

The highest and best use of a non-financial asset takes into account the use of the asset that is physically possible, legally permissible and financially feasible, as follows:

(a) A use that is physically possible takes into account the physical characteristics of the asset that market participants would take into account when pricing the asset (eg the location or size of a property).

(b) A use that is legally permissible takes into account any legal restrictions on the use of the asset that market participants would take into account when pricing the asset (eg the zoning regulations applicable to a property).

(c) A use that is financially feasible takes into account whether a use of the asset that is physically possible and legally permissible generates adequate income or cash flows (taking into account the costs of converting the asset to that use) to produce an investment return that market participants would require from an investment in that asset put to that use.

Highest and best use is determined from the perspective of market participants, even if the entity intends a different use. However, an entity's current use of a non-financial asset is presumed to be its highest and best use unless market or other factors suggest that a different use by market participants would maximise the value of the asset.

To protect its competitive position, or for other reasons, an entity may intend not to use an acquired non-financial asset actively or it may intend not to use the asset according to its highest and best use. Nevertheless, the entity shall measure the fair value of a non-financial asset assuming its highest and best use by market participants.

In the given case, the highest best possible use of the land is to develop a commercial complex. Although developing a business complex is against the business objective of the entity, it does not affect the basis of fair valuation as Ind AS 113 does not consider an entity specific restriction for measuring the fair value.

Also, its current use as a parking lot is not the highest best use as the land has the potential of being used for building a commercial complex.

Therefore, the fair value of the land is the price that would be received when sold to a market participant who is interested in developing a commercial complex.

(ii) As per Ind AS 113, unobservable inputs shall be used to measure fair value to the extent that relevant observable inputs are not available, thereby allowing for situations in which there is little, if any, market activity for the asset or liability at the measurement date. The unobservable inputs shall reflect the assumptions that market participants would use when pricing the asset or liability, including assumptions about risk.

© The Institute of Chartered Accountants of India

In the given case, DS Limited adopted discounted cash flow method, commonly used technique to value shares, to fair value the shares of the private company as there were no similar shares traded in the market. Hence, it falls under Level 3 of fair value hierarchy.

Level 2 inputs include the following:

(a) quoted prices for similar assets or liabilities in active markets.

(b) quoted prices for identical or similar assets or liabilities in markets that are not active.

(c) inputs other than quoted prices that are observable for the asset or liability.

If an entity can access quoted price in active markets for identical assets or liabilities of similar companies which can be used for fair valuation of the shares without any adjustment, at the measurement date, then it will be considered as observable input and would be considered as Level 2 inputs.

7.

		Amount (In Crore)
Expected Labour Cost (Refer W.N.)		131.25
Allocated Overheads	(80% x 131.25 Cr)	105.00
Profit markup on Cost	(131.25 + 105) x 20%	47.25
Total Expected Cash Flows before inflation		**283.50**
Inflation factor for next 10 years (4%)	$(1.04)^{10}$ =1.4802	
Expected cash flows adjusted for inflation	283.50 x 1.4802	419.65
Risk adjustment - uncertainty relating to cash flows	(5% x 419.64)	20.98
Total Expected Cash Flows	(419.65+20.98)	440.63
Discount rate to be considered = risk-free rate + entity's non-performance risk	5% + 3.5%	8.5%
Expected present value at 8.5% for 10 years	**(440.63 / (1.085^{10}))**	**194.97**

Working Note:

Expected labour cost:

Cash Flows Estimates	Probability	Expected Cash Flows
100 Cr	25%	25 Cr
125 Cr	50%	62.50 Cr
175 Cr	25%	43.75 Cr
Total		**131.25 Cr**

© The Institute of Chartered Accountants of India

8. (i) An earnings-based valuation of Entity A's holding of shares in company XYZ could be calculated as follows:

Particulars	**Unit**
Entity XYZ's after-tax maintainable profits (A)	₹ 70,000
Price/Earnings ratio (B)	15
Adjusted discount factor (C) (1- 0.20)	0.80
Value of Company XYZ (A) x (B) x (C)	₹ 8,40,000

Value of a share of XYZ = ₹ 8,40,000 ÷ 5,000 shares = ₹ 168

The fair value of Entity A's investment in XYZ's shares is estimated at ₹ 42,000 (that is, 250 shares x ₹ 168 per share).

(ii) Share price = ₹ 8,50,000 ÷ 5,000 shares = ₹ 170 per share.

The fair value of Entity A's investment in XYZ shares is estimated to be ₹ 42,500 (250 shares x ₹ 170 per share).

© The Institute of Chartered Accountants of India

FOR SHORTCUT TO IND AS WISDOM: SCAN ME!

TEST YOUR KNOWLEDGE

Questions

1. Q TV released an advertisement in Deshabandhu, a vernacular daily. Instead of paying for the same, Q TV allowed Deshabandhu a free advertisement spot, which was duly utilised by Deshabandu. How revenue for these non-monetary transactions in the area of advertising will be recognized and measured?

2. A Ltd. a telecommunication company, entered into an agreement with B Ltd. which is engaged in generation and supply of power. The agreement provided that A Ltd. will provide 1,00,000 minutes of talk time to employees of B Ltd. in exchange for getting power equivalent to 20,000 units. A Ltd. normally charges ₹ 0.50 per minute and B Ltd. charges ₹ 2.5 per unit. How should revenue be measured in this case?

3. Company X enters into an agreement on 1st January, 20X1 with a customer for renovation of hospital and install new air-conditioners for total consideration of ₹ 50,00,000. The promised renovation service, including the installation of new air-conditioners is a single performance obligation satisfied over time. Total expected costs are ₹ 40,00,000 including ₹ 10,00,000 for the air conditioners.

   Company X determines that it acts as a principal in accordance with paragraphs B34-B38 of Ind AS 115 because it obtains control of the air conditioners before they are transferred to the customer. The customer obtains control of the air conditioners when they are delivered to the hospital premises.

   Company X uses an input method based on costs incurred to measure its progress towards complete satisfaction of the performance obligation.

© The Institute of Chartered Accountants of India

As at 31st March, 20X1, other costs incurred excluding the air conditioners are ₹ 6,00,000.

Whether Company X should include cost of the air conditioners in measure of its progress of performance obligation? How should revenue be recognized for the year ended March 20X1?

4. An entity G Ltd. enters into a contract with a customer P Ltd. for the sale of a machinery for ₹ 20,00,000. P Ltd. intends to use the said machinery to start a food processing unit. The food processing industry is highly competitive and P Ltd. has very little experience in the said industry.

   P Ltd. pays a non-refundable deposit of ₹ 1,00,000 at inception of the contract and enters into a long-term financing agreement with G Ltd. for the remaining 95 per cent of the agreed consideration which it intends to pay primarily from income derived from its food processing unit as it lacks any other major source of income. The financing arrangement is provided on a non-recourse basis, which means that if P Ltd. defaults then G Ltd. can repossess the machinery but cannot seek further compensation from P Ltd., even if the full value of the amount owed is not recovered from the machinery. The cost of the machinery for G Ltd. is ₹ 12,00,000. P Ltd. obtains control of the machinery at contract inception.

   When should G Ltd. recognize revenue from sale of machinery to P Ltd. in accordance with Ind AS 115?

5. Entity I sells a piece of machinery to the customer for ₹ 2 million, payable in 90 days. Entity I is aware at contract inception that the customer might not pay the full contract price. Entity I estimates that the customer will pay atleast ₹ 1.75 million, which is sufficient to cover entity I's cost of sales (₹ 1.5 million) and which entity I is willing to accept because it wants to grow its presence in this market. Entity I has granted similar price concessions in comparable contracts.

   Entity I concludes that it is highly probable that it will collect ₹ 1.75 million, and such amount is not constrained under the variable consideration guidance.

   What is the transaction price in this arrangement?

6. On 1st January 20X8, entity J enters into a one-year contract with a customer to deliver water treatment chemicals. The contract stipulates that the price per container will be adjusted retroactively once the customer reaches certain sales volume, defined, as follows:

Price per container	Cumulative sales volume
₹ 100	1 - 1,000,000 containers
₹ 90	1,000,001 - 3,000,000 containers
₹ 85	3,000,001 containers and above

© The Institute of Chartered Accountants of India

Volume is determined based on sales during the calendar year. There are no minimum purchase requirements. Entity J estimates that the total sales volume for the year will be 2.8 million containers, based on its experience with similar contracts and forecasted sales to the customer.

Entity J sells 700,000 containers to the customer during the first quarter ended 31st March 20X8 for a contract price of ₹ 100 per container.

How should entity J determine the transaction price?

7. Entity K sells electric razors to retailers for C 50 per unit. A rebate coupon is included inside the electric razor package that can be redeemed by the end consumers for C 10 per unit.

   Entity K estimates that 20% to 25% of eligible rebates will be redeemed, based on its experience with similar programmes and rebate redemption rates available in the market for similar programmes. Entity K concludes that the transaction price should incorporate an assumption of 25% rebate redemption, as this is the amount for which it is highly probable that a significant reversal of cumulative revenue will not occur if estimates of the rebates change.

   How should entity K determine the transaction price?

8. A manufacturer enters into a contract to sell goods to a retailer for ₹ 1,000. The manufacturer also offers price protection, whereby it will reimburse the retailer for any difference between the sale price and the lowest price offered to any customer during the following six months. This clause is consistent with other price protection clauses offered in the past, and the manufacturer believes that it has experience which is predictive for this contract.

   Management expects that it will offer a price decrease of 5% during the price protection period. Management concludes that it is highly probable that a significant reversal of cumulative revenue will not occur if estimates change.

   How should the manufacturer determine the transaction price?

9. Electronics Manufacturer M sells 1,000 televisions to Retailer R for ₹ 50,00,000 (₹ 5,000 per television). M provides price protection to R by agreeing to reimburse R for the difference between this price and the lowest price that it offers for that television during the following six months. Based on M's extensive experience with similar arrangements, it estimates the following outcomes.

Price reduction in next six months (₹)	Probability
0	70%

© The Institute of Chartered Accountants of India

₹ 500	20%
₹ 1,000	10%

Determine the transaction price.

10. Construction Company C enters into a contract with Customer E to build an asset. Depending on when the asset is completed, C will receive either ₹ 1,10,000 or ₹ 1,30,000.

Outcome	Consideration (₹)	Probability
Project completes on time	1,30,000	90%
Project is delayed	1,10,000	10%

Determine the transaction price.

11. Franchisor Y Ltd. licenses the right to operate a store in a specified location to Franchisee F. The store bears Y Ltd.'s trade name and F will have a right to sell Y Ltd.'s products for 10 years. F pays an up-front fixed fee. The franchise contract also requires Y Ltd. to maintain the brand through product improvements, marketing campaigns etc. Determine the nature of license.

Answers

1. Paragraph 5(d) of Ind AS 115 excludes non-monetary exchanges between entities in the same line of business to facilitate sales to customers or potential customers. For example, this Standard would not apply to a contract between two oil companies that agree to an exchange of oil to fulfil demand from their customers in different specified locations on a timely basis.

In industries with homogenous products, it is common for entities in the same line of business to exchange products in order to sell them to customers or potential customers other than parties to exchange. The current scenario, on the contrary, will be covered under Ind AS 115 since the same is exchange of dissimilar goods or services because both of the entities deal in different mode of media, i.e., one is print media and another is electronic media and both parties are acting as customers and suppliers for each other.

Further, in the current scenario, it seems it is for consumption by the said parties and hence it does not fall under paragraph 5(d). It may also be noted that, even if it was to facilitate sales to customers or potential customers, it would not be scoped out since the parties are not in the same line of business.

As per paragraph 47 of Ind AS 115, "An entity shall consider the terms of the contract and

© The Institute of Chartered Accountants of India

its customary business practices to determine the transaction price. The transaction price is the amount of consideration to which an entity expects to be entitled in exchange for transferring promised goods or services to a customer, excluding amounts collected on behalf of third parties (for example, some sales taxes). The consideration promised in a contract with a customer may include fixed amounts, variable amounts, or both".

Paragraph 66 of Ind AS 115 provides that to determine the transaction price for contracts in which a customer promises consideration in a form other than cash, an entity shall measure the non-cash consideration (or promise of non-cash consideration) at fair value.

In accordance with the above, Q TV and Deshabandhu should measure the revenue promised in the form of non-cash consideration as per the above referred principles of Ind AS 115.

2. Paragraph 5(d) of Ind AS 115 excludes non-monetary exchanges between entities in the same line of business to facilitate sales to customers or potential customers. For example, this Standard would not apply to a contract between two oil companies that agree to an exchange of oil to fulfil demand from their customers in different specified locations on a timely basis.

However, the current scenario will be covered under Ind AS 115 since the same is exchange of dissimilar goods or services.

As per paragraph 47 of Ind AS 115, "an entity shall consider the terms of the contract and its customary business practices to determine the transaction price. The transaction price is the amount of consideration to which an entity expects to be entitled in exchange for transferring promised goods or services to a customer, excluding amounts collected on behalf of third parties (for example, some sales taxes). The consideration promised in a contract with a customer may include fixed amounts, variable amounts, or both".

Paragraph 66 of Ind AS 115 provides that to determine the transaction price for contracts in which a customer promises consideration in a form other than cash, an entity shall measure the non-cash consideration (or promise of noncash consideration) at fair value.

On the basis of the above, revenue recognized by A Ltd. will be the consideration in the form of power units that it expects to be entitled for talktime sold, i.e. ₹ 50,000 (20,000 units x ₹ 2.5). The revenue recognized by B Ltd. will be the consideration in the form of talk time that it expects to be entitled for the power units sold, i.e., ₹ 50,000 (1,00,000 minutes x ₹ 0.50).

3. Paragraph B19 of Ind AS 115 inter alia, states that, "an entity shall exclude from an input method the effects of any inputs that, in accordance with the objective of measuring

© The Institute of Chartered Accountants of India

progress in paragraph 39, do not depict the entity's performance in transferring control of goods or services to the customer".

In accordance with the above, Company X assesses whether the costs incurred to procure the air conditioners are proportionate to the entity's progress in satisfying the performance obligation. The costs incurred to procure the air conditioners (₹ 10,00,000) are significant relative to the total costs to completely satisfy the performance obligation (₹ 40,00,000). Also, Company X is not involved in manufacturing or designing the air conditioners.

Company X concludes that including the costs to procure the air conditioners in the measure of progress would overstate the extent of the entity's performance. Consequently, in accordance with paragraph B19 of Ind AS 115, the entity adjusts its measure of progress to exclude the costs to procure the air conditioners from the measure of costs incurred and from the transaction price. The entity recognizes revenue for the transfer of the air conditioners at an amount equal to the costs to procure the air conditioners (i.e., at a zero margin).

Company X assesses that as at March, 20X1, the performance is 20 per cent complete (i.e., ₹ 6,00,000 / ₹ 30,00,000). Consequently, Company X recognizes the following-

As at 31st March, 20X1

	Amount in ₹
Revenue	18,00,000
Cost of goods sold	16,00,000
Profit	2,00,000

Revenue recognized is calculated as (20 per cent × ₹ 40,00,000) + ₹ 10,00,000.

(₹ 40,00,000 = ₹ 50,00,000 transaction price – ₹ 10,00,000 costs of air conditioners.)

Cost of goods sold is ₹ 6,00,000 of costs incurred + ₹ 10,00,000 costs of air conditioners.

4. As per paragraph 9 of Ind AS 115, "An entity shall account for a contract with a customer that is within the scope of this Standard only when all of the following criteria are met:

(a) the parties to the contract have approved the contract (in writing, orally or in accordance with other customary business practices) and are committed to perform their respective obligations;

(b) the entity can identify each party's rights regarding the goods or services to be transferred;

(c) the entity can identify the payment terms for the goods or services to be transferred;

© The Institute of Chartered Accountants of India

(d) the contract has commercial substance (ie the risk, timing or amount of the entity's future cash flows is expected to change as a result of the contract); and

(e) it is probable that the entity will collect the consideration to which it will be entitled in exchange for the goods or services that will be transferred to the customer. In evaluating whether collectability of an amount of consideration is probable, an entity shall consider only the customer's ability and intention to pay that amount of consideration when it is due. The amount of consideration to which the entity will be entitled may be less than the price stated in the contract if the consideration is variable because the entity may offer the customer a price concession".

Paragraph 9(e) above, requires that for revenue to be recognized, it should be probable that the entity will collect the consideration to which it will be entitled in exchange for the goods or services that will be transferred to the customer. In the given case, it is not probable that G Ltd. will collect the consideration to which it is entitled in exchange for the transfer of the machinery. P Ltd.'s ability to pay may be uncertain due to the following reasons:

(a) P Ltd. intends to pay the remaining consideration (which has a significant balance) primarily from income derived from its food processing unit (which is a business involving significant risk because of high competition in the said industry and P Ltd.'s little experience);

(b) P Ltd. lacks sources of other income or assets that could be used to repay the balance consideration; and

(c) P Ltd.'s liability is limited because the financing arrangement is provided on a non-recourse basis.

In accordance with the above, the criteria in paragraph 9 of Ind AS 115 are not met.

Further, para 15 states that when a contract with a customer does not meet the criteria in paragraph 9 and an entity receives consideration from the customer, the entity shall recognize the consideration received as revenue only when either of the following events has occurred:

(a) the entity has no remaining obligations to transfer goods or services to the customer and all, or substantially all, of the consideration promised by the customer has been received by the entity and is non-refundable; or

(b) the contract has been terminated and the consideration received from the customer is non-refundable.

Para 16 states that an entity shall recognize the consideration received from a customer as a liability until one of the events in paragraph 15 occurs or until the criteria in paragraph 9

© The Institute of Chartered Accountants of India

are subsequently met. Depending on the facts and circumstances relating to the contract, the liability recognized represents the entity's obligation to either transfer goods or services in the future or refund the consideration received. In either case, the liability shall be measured at the amount of consideration received from the customer.

In accordance with the above, in the given case G Ltd. should account for the non-refundable deposit of ₹ 1,00,000 payment as a deposit liability as none of the events described in paragraph 15 have occurred—that is, neither the entity has received substantially all of the consideration, nor it has terminated the contract. Consequently, in accordance with paragraph 16, G Ltd. will continue to account for the initial deposit as well as any future payments of principal and interest as a deposit liability until the criteria in paragraph 9 are met (i.e. the entity is able to conclude that it is probable that the entity will collect the consideration) or one of the events in paragraph 15 has occurred. Further, G Ltd. will continue to assess the contract in accordance with paragraph 14 to determine whether the criteria in paragraph 9 are subsequently met or whether the events in paragraph 15 of Ind AS 115 have occurred.

5. Entity I is likely to provide a price concession and accept an amount less than ₹ 2 million in exchange for the machinery. The consideration is therefore variable. The transaction price in this arrangement is ₹ 1.75 million, as this is the amount which entity I expects to receive after providing the concession and it is not constrained under the variable consideration guidance. Entity I can also conclude that the collectability threshold is met for ₹ 1.75 million and therefore contract exists.

6. The transaction price is ₹ 90 per container based on entity J's estimate of total sales volume for the year, since the estimated cumulative sales volume of 2.8 million containers would result in a price per container of ₹ 90. Entity J concludes that based on a transaction price of ₹ 90 per container, it is highly probable that a significant reversal in the amount of cumulative revenue recognized will not occur when the uncertainty is resolved. Revenue is therefore recognized at a selling price of ₹ 90 per container as each container is sold. Entity J will recognize a liability for cash received in excess of the transaction price for the first 1 million containers sold at ₹ 100 per container (that is, ₹ 10 per container) until the cumulative sales volume is reached for the next pricing tier and the price is retroactively reduced.

For the quarter ended 31st March, 20X8, entity J recognizes revenue of ₹ 63 million (700,000 containers x ₹ 90) and a liability of ₹ 7 million [700,000 containers x (₹ 100 - ₹ 90)].

Entity J will update its estimate of the total sales volume at each reporting date until the uncertainty is resolved.

7. Entity K records sales to the retailer at a transaction price of ₹ 47.50 (₹ 50 less 25% of ₹ 10). The difference between the per unit cash selling price to the retailers and the

© The Institute of Chartered Accountants of India

transaction price is recorded as a liability for cash consideration expected to be paid to the end customer. Entity K will update its estimate of the rebate and the transaction price at each reporting date if estimates of redemption rates change.

8. The transaction price is ₹ 950, because the expected reimbursement is ₹ 50. The expected payment to the retailer is reflected in the transaction price at contract inception, as that is the amount of consideration to which the manufacturer expects to be entitled after the price protection. The manufacturer will recognize a liability for the difference between the invoice price and the transaction price, as this represents the cash that it expects to refund to the retailer. The manufacturer will update its estimate of expected reimbursement at each reporting date until the uncertainty is resolved.

9. After considering all relevant facts and circumstances, M determines that the expected value method provides the best prediction of the amount of consideration to which it will be entitled. As a result, it estimates the transaction price to be ₹ 4,800 per television – i.e. (₹ 5,000 x 70%) + (₹ 4,500 x 20%) + (₹ 4,000 x 10%).

10. Because there are only two possible outcomes under the contract, C determines that using the most likely amount provides the best prediction of the amount of consideration to which it will be entitled. C estimates the transaction price to be ₹ 1,30,000, which is the single most likely amount.

11. The licence provides F access to the IP as it exists at any point in time in the licence period. This is because:

- Y Ltd. is required to maintain the brand, which will significantly affect the IP by affecting F's ability to obtain benefit from the brand;
- any action by Y Ltd. may have a direct positive or negative effect on F; and
- these activities do not transfer a goods or service to F.

Therefore, Y Ltd. recognizes the up-front fee over the 10-year franchise period.

© The Institute of Chartered Accountants of India

FOR SHORTCUT TO IND AS WISDOM: SCAN ME!

TEST YOUR KNOWLEDGE

Questions

1. UA Ltd. purchased raw material @ ₹ 400 per kg. Company does not sell raw material but uses in production of finished goods. The finished goods in which raw material is used are expected to be sold at below cost. At the end of the accounting year, company is having 10,000 kg of raw material in inventory. As the company never sells the raw material, it does not know the selling price of raw material and hence cannot calculate the realisable value of the raw material for valuation of inventories at the end of the year. However, replacement cost of raw material is ₹ 300 per kg. Compute the value of inventory of raw material?

2. Sun Ltd. has fabricated special equipment (solar power panel) during 20X1-20X2 as per drawing and design supplied by the customer. However, due to a liquidity crunch, the customer has requested the company for postponement in delivery schedule and requested the company to withhold the delivery of finished goods products and discontinue the production of balance items.

   As a result of the above, the details of customer balance and the goods held by the company as work-in-progress and finished goods as on 31.3.20X3 are as follows:

Solar power panel (WIP)	₹ 85 lakhs
Solar power panel (finished products)	₹ 55 lakhs
Sundry Debtor (solar power panel)	₹ 65 lakhs

   The petition for winding up against the customer has been filed during 20X2-20X3 by Sun Ltd. Advise on provision to be made of ₹ 205 lakh included in Sundry Debtors, Finished goods and work-in-progress in the financial statement of 20X2-20X3.

© The Institute of Chartered Accountants of India

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

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

   Determine the value inventory at the following dates:

   (a) 31st March 20X1

   (b) 31st March 20X2

4. The following information is gathered from an entity:

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

   Determine the overhead costs to be allocated to cost of goods sold and closing inventory?

5. Sharp Trading Inc. purchases motorcycles from various countries and exports them to Europe. Sharp Trading has incurred these expenses during 20X1:

   (a) Cost of purchases (based on vendors' invoices) ₹ 5,00,000

   (b) Trade discounts on purchases ₹ 10,000

   (c) Import duties ₹ 200

   (d) Freight and insurance on purchases ₹ 250

© The Institute of Chartered Accountants of India

(e) Other handling costs relating to imports ₹ 100

(f) Salaries of accounting department ₹ 15,000

(g) Brokerage commission payable to indenting agents for arranging imports ₹ 300

(h) Sales commission payable to sales agents ₹ 150

(i) After-sales warranty costs ₹ 600

Advise as if which of the above item is to be included in the cost of inventory and wants you to calculate cost of inventory as per Ind AS 2.

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

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

During January 20X1 the entity designed the corporate gifts for the customer.

Design costs included:

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

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

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

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

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

The customised corporate gifts were ready for sale on 1st March 20X1. No abnormal wastage occurred in the development and manufacture of the corporate gifts.

Compute the cost of the inventory? Substantiate your answer with appropriate reasons and calculations, wherever required.

© The Institute of Chartered Accountants of India

Answers

1. As per Ind AS 2 "Inventories", materials and other supplies held for use in the production of inventories are not written down below cost if the finished products in which they will be incorporated are expected to be sold at or above cost. However, when there has been a decline in the price of materials and it is estimated that the cost of the finished products will exceed net realisable value, the materials are written down to net realisable value. In such circumstances, the replacement cost of the materials may be the best available measure of their net realisable value. Therefore, in this case, UA Ltd. will value the inventory of raw material at ₹ 30,00,000 (10,000 kg. @ ₹ 300 per kg.).

2. From the facts given in the question it is obvious that Sun Ltd. is a manufacturer of solar power panel. As per Ind AS 2 'Inventories', inventories are assets (a) held for sale in the ordinary course of business; (b) in the process of production for such sale; or (c) in the form of materials or supplies to be consumed in the production process or in the rendering of services. Therefore, solar power panel held in its stock will be considered as its inventory. Further, as per the standard, inventory at the end of the year is to be valued at lower of cost or NRV.

   As the customer has postponed the delivery schedule due to liquidity crunch the entire cost incurred for solar power panel which were to be supplied has been shown in Inventory. The solar power panel are in the possession of the Company which can be sold in the market. Hence, the company should value such inventory as per principle laid down in Ind AS 2 i.e. lower of Cost or NRV. Though, the goods were produced as per specifications of buyer the Company should determine the NRV of these goods in the market and value the goods accordingly. Change in value of such solar power panel should be provided for in the books. In the absence of the NRV of WIP and Finished product given in the question, assuming that cost is lower, the company shall value its inventory as per Ind AS 2 for ₹ 140 lakhs [i.e solar power panel (WIP) ₹ 85 lakhs + solar power panel (finished products) ₹ 55 lakhs].

   Alternatively, if it is assumed that there is no buyer for such fabricated solar power panel, then the NRV will be Nil. In such a case, full value of finished goods and WIP will be provided for in the books.

   As regards Sundry Debtors balance, since the Company has filed a petition for winding up against the customer in 20X2-20X3, it is probable that amount is not recoverable from the party. Hence, the provision for doubtful debts for ₹ 65 lakhs shall be made in the books against the debtor's amount.

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

© The Institute of Chartered Accountants of India

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

(b) As per para 33 of Ind AS 2, a new assessment is made of net realisable value in each subsequent period. It *inter alia* states that if there is increase in net realisable value because of changed economic circumstances, the amount of write down is reversed so that new carrying amount is the lower of the cost and the revised net realisable value. Accordingly, as at 31 March 20X2, again inventory would be valued at cost or net realisable value whichever is lower. In the present case, cost is ₹ 10 million and net realisable value would be ₹ 10.5 million (i.e. expected selling price ₹ 11 million – estimated selling expense ₹ 0.5 million). Accordingly, inventory would be recorded at ₹ 10 million and inventory write down carried out in previous year for ₹ 2.5 million shall be reversed.

4. **Hours taken to produce 1 unit** = 6,500 hours / 6,500 units = 1 hour per unit.

Fixed production overhead absorption rate:

= Fixed production overhead / labour hours for normal capacity

= ₹ 1,500 / 7,500

= ₹ 0.2 per hour

Management should allocate fixed overhead costs to units produced at a rate of ₹ 0.2 per hour.

Therefore, fixed production overhead allocated to 6,500 units produced during the year (one unit per hour) = 6,500 units x1 hour x ₹ 0.2 = ₹ 1,300.

The remaining fixed overhead incurred during the year of ₹ 200 (₹ 1500 – ₹ 1300) that remains unallocated is recognized as an expense.

The amount of fixed overhead allocated to inventory is not increased as a result of low production by using normal capacity to allocate fixed overhead.

Variable production overhead absorption rate:

= Variable production overhead/actual hours for current period

= ₹ 2,600 / 6,500 hours

= ₹ 0.4 per hour

Management should allocate variable overhead costs to units produced at a rate of ₹ 0.4 per hour.

© The Institute of Chartered Accountants of India

The above rate results in the allocation of all variable overheads to units produced during the year.

Closing inventory = Opening inventory + Units produced during year – Units sold during year

= 2,500 + 6,500 – 6,700 = 2,300 units

As each unit has taken one hour to produce (6,500 hours / 6,500 units produced), total fixed and variable production overhead recognized as part of cost of inventory:

= Number of units of closing inventory x Number of hours to produce each unit x (Fixed production overhead absorption rate + Variable production overhead absorption rate)

= 2,300 units x 1 hour x (₹ 0.2 + ₹ 0.4)

= ₹ 1,380

The remaining ₹ 2,720 [(₹ 1,500 + ₹ 2,600) – ₹ 1,380] is recognized as an expense in the income statement as follows:

	₹
Absorbed in cost of goods sold (FIFO basis) (6,500 – 2,300) = 4,200 x ₹ 0.6	2,520
Unabsorbed fixed overheads, not included in the cost of goods sold	200
Total	**2,720**

5. Items (a), (b), (c), (d), (e), and (g) are permitted to be included in the cost of inventory since these elements contribute to cost of purchase, cost of conversion and other costs incurred in bringing the inventories to their present location and condition, as per Ind AS 2

Statement showing cost of inventory

	₹
Cost of purchases (based on vendors' invoices)	5,00,000
Trade discounts on purchases	(10,000)
Import duties	200
Freight and insurance on purchases	250
Other handling costs relating to imports	100
Brokerage commission payable to indenting agents for arranging imports	300
Cost of inventory under Ind AS 2	4,90,850

Note: Salaries of accounting department, sales commission, and after-sales warranty costs are not considered as part of cost of inventory under Ind AS 2.

© The Institute of Chartered Accountants of India

6. Statement showing computation of inventory cost

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

Working Note:

Costs of testing product designed for specific customer:

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

© The Institute of Chartered Accountants of India

FOR SHORTCUT TO IND AS WISDOM: SCAN ME!

TEST YOUR KNOWLEDGE

Questions

1. ABC Ltd. is installing a new plant at its production facility. It has incurred these costs:

1.	Cost of the plant (cost per supplier's invoice plus taxes)	₹ 25,00,000
2.	Initial delivery and handling costs	₹ 2,00,000
3.	Cost of site preparation	₹ 6,00,000
4.	Consultants used for advice on the acquisition of the plant	₹ 7,00,000
5.	Interest charges paid to supplier of plant for deferred credit	₹ 2,00,000
6.	Net present value of estimated dismantling costs to be incurred after 7 years	₹ 3,00,000
7.	Operating losses before commercial production	₹ 4,00,000

Advise ABC Ltd. on the costs that can be capitalized in accordance with Ind AS 16.

2. A Ltd. has an item of property, plant and equipment with an initial cost of ₹ 1,00,000. At the date of revaluation, accumulated depreciation amounted to ₹ 55,000. The fair value of the asset, by reference to transactions in similar assets, is assessed to be ₹ 65,000.

   Pass journal entries with regard to revaluation.

3. B Ltd. owns an asset with an original cost of ₹ 2,00,000. On acquisition, management determined that the useful life was 10 years and the residual value would be ₹ 20,000. The asset is now 8 years old, and during this time there have been no revisions to the assessed residual value.

© The Institute of Chartered Accountants of India

At the end of year 8, management has reviewed the useful life and residual value and has determined that the useful life can be extended to 12 years in view of the maintenance program adopted by the company. As a result, the residual value will reduce to ₹ 10,000.

Analyze how would the above changes in estimates be accounted by B Ltd.

4. X Ltd. has a machine which got damaged due to fire as on 31st January, 20X1. The carrying amount of machine was ₹ 1,00,000 on that date. X Ltd. sold the damaged asset as scrap for ₹ 10,000. X Ltd. has insured the same asset against damage. As on 31st March, 20X1, the compensation proceedings were still in process but the insurance company has confirmed the claim. Compensation of ₹ 50,000 is receivable from the insurance company.

   Determine the accounting for the above transaction for X Ltd.

5. An entity has a nuclear power plant and a related decommissioning liability. The nuclear power plant started operating on 1st April, 2XX1. The plant has a useful life of 40 years. Its initial cost was ₹ 1,20,000 which included an amount for decommissioning costs of ₹ 10,000, which represented ₹ 70,400 in estimated cash flows payable in 40 years discounted at a risk-adjusted rate of 5 per cent. The entity's financial year ends on 31st March. After 10 years, the net present value of the decommissioning liability has decreased by ₹ 8,000. The discount rate has not yet changed.

   Examine how the entity will account for the above changes in decommissioning liability in the 11th year, if it adopts cost model.

6. An entity has a nuclear power plant and a related decommissioning liability. The nuclear power plant started operating on 1st April, 20X1. The plant has a useful life of 40 years. Its initial cost was ₹ 1,20,000. This included an amount for decommissioning costs of ₹ 10,000, which represented ₹ 70,400 in estimated cash flows payable in 40 years discounted at a risk-adjusted rate of 5 per cent. The entity's financial year ends on 31st March. Assume that a market-based discounted cash flow valuation of ₹ 1,15,000 is obtained at 31st March, 20X4. This valuation is after deduction of an allowance of ₹ 11,600 for decommissioning costs, which represents no change to the original estimate, after the unwinding of three years' discount. On 31st March, 20X5, the entity estimates that, as a result of technological advances, the present value of the decommissioning liability has decreased by ₹ 5,000. The entity decides that a full valuation of the asset is needed at 31st March, 20X5, in order to ensure that the carrying amount does not differ materially from fair value. The asset is now valued at ₹ 1,07,000, which is net of an allowance for the reduced decommissioning obligation.

   Examine how will the entity account for the above changes in decommissioning liability if it adopts revaluation model.

© The Institute of Chartered Accountants of India

7. A Ltd. purchased some Property, Plant and Equipment on 1st April, 20X1, and estimated their useful lives for the purpose of financial statements prepared on the basis of Ind AS. Following were the original cost, and useful life of the various components of property, plant, and equipment assessed on 1st April, 20X1:

Property, Plant and Equipment	Original Cost	Estimated useful life
Buildings	₹ 15,000,000	15 years
Plant and machinery	₹ 10,000,000	10 years
Furniture and fixtures	₹ 3,500,000	7 years

A Ltd. uses the straight-line method of depreciation. On 1st April, 20X4, the entity reviewed the following useful lives of the property, plant, and equipment through an external valuation expert:

Buildings	10 years
Plant and machinery	7 years
Furniture and fixtures	5 years

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

Examine the impact of revaluation of useful life on the Statement of Profit and Loss for the year ending 31st March, 20X5.

8. Mr. X, is the financial controller of ABC Ltd., a listed entity which prepares consolidated financial statements in accordance with Ind AS. Mr. X has recently produced the final draft of the financial statements of ABC Ltd. for the year ended 31st March, 20X1 to the managing director Mr. Y for approval. Mr. Y, who is not an accountant, had raised following query from Mr. X after going through the draft financial statements:

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

Advise the finance controller for resolving the query of the managing director?

© The Institute of Chartered Accountants of India

9. Company X performed a revaluation of all of its plant and machinery at the beginning of 20X1. The following information relates to one of the machinery:

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

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

Advise how should the company account for revaluation of plant and machinery and depreciation subsequent to revaluation. Support your answer with journal entries.

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

- Property A — a vacant plot of land on which it intends to construct its new administration headquarters;
- Property B — a plot of land that it operates as a landfill site;
- Property C — a plot of land on which its existing administration headquarters are built;
- Property D — a plot of land on which its direct sales office is built;
- Properties E1–E10 — ten separate retail outlets and the land on which they are built;
- Equipment A — computer systems at its headquarters and direct sales office that are integrated with the point of sale computer systems in the retail outlets;
- Equipment B — point of sale computer systems in each of its retail outlets;
- Furniture and fittings in its administrative headquarters and its sales office;
- Shop fixtures and fittings in its retail outlets.

Determine the classes of property, plant and equipment for disclosure by the entity?

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

© The Institute of Chartered Accountants of India

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

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

Answers

1. According to Ind AS 16, these costs can be capitalized:

1.	Cost of the plant	₹ 25,00,000
2.	Initial delivery and handling costs	₹ 2,00,000
3.	Cost of site preparation	₹ 6,00,000
4.	Consultants' fees	₹ 7,00,000
5.	Net present value of estimated dismantling costs to be incurred after 7 years	₹ 3,00,000
		₹ 43,00,000

Note: Interest charges paid on "Deferred credit terms" to the supplier of the plant (not a qualifying asset) of ₹ 2,00,000 and operating losses before commercial production amounting to ₹ 4,00,000 are not regarded as directly attributable costs and thus cannot be capitalized. They should be written off to the Statement of Profit and Loss in the period they are incurred.

2. The entries to be passed would be:

	₹	₹
Accumulated depreciation Dr. To Asset A/c (Being elimination of accumulated depreciation against the cost of the asset)	55,000	 55,000
Asset A/c Dr To Revaluation Surplus (Being increase of net asset value to Fair value)	20,000	 20,000

Note: The net result is that the asset has a carrying amount of ₹ 65,000 [1,00,000 – 55,000 + 20,000.]

© The Institute of Chartered Accountants of India

3. Calculation of accumulated depreciation till 8th year

Depreciable amount {Cost less residual value} = ₹ 2,00,000 – ₹ 20,000 = ₹ 1,80,000.

Annual depreciation = Depreciable amount / Useful life = 1,80,000 / 10 = ₹ 18,000.

Accumulated depreciation = 18,000 x No. of years (8) = ₹ 1,44,000.

Calculation of carrying amount at the end of the 8th year

The asset has a carrying amount of ₹ 56,000 at the end of year 8 [ie. ₹ 2,00,000 – ₹ 1,44,000]

Accounting of the changes in estimates

Revision of the useful life to 12 years results in a remaining useful life of 4 years (ie 12 years – 8 years).

The revised depreciable amount is ₹ 46,000 (₹ 56,000 – ₹ 10,000)

Thus, depreciation should be charged in future ie from 9th year onwards at ₹ 11,500 per annum (₹ 46,000 / 4 years).

4. As per para 66 of Ind AS 16, impairment or losses of items of property, plant and equipment and related claims for or payments of compensation from third parties are separate economic events and should be accounted for separately.

X Ltd. should account for the above transaction as given below:

At the time of sale of scrap machine, X Ltd. should write off the carrying amount of asset from books of account and provide a loss of ₹ 90,000. (i.e., carrying amount of ₹ 1,00,000 – realised amount of ₹ 10,000)

As on 31st March, 20X1, X Ltd. should recognize income of ₹ 50,000 against the compensation receivable in its profit or loss.

5. On 31st March, 2X11, the plant is 10 years old. Accumulated depreciation is ₹ 30,000 (₹ 120,000 x 10 / 40 years). Due to unwinding of discount @ 5% over the 10 years, the amount of decommissioning liability has increased from ₹ 10,000 to ₹ 16,300 (approx.).

On 31st March, 2X11, the discount rate has not changed. However, the entity estimates that, as a result of technological advances, the net present value of the decommissioning liability has decreased by ₹ 8,000. Accordingly, the entity adjusts the decommissioning liability from ₹ 16,300 to ₹ 8,300. On this date, the entity passes the following journal entry to reflect the change:

© The Institute of Chartered Accountants of India

		₹	₹
Provision for decommissioning liability	Dr.	8,000	
To Asset			8,000

Following this adjustment, the carrying amount of the asset is ₹ 82,000 (₹ 1,20,000 – ₹ 8,000 – ₹ 30,000), which will be depreciated over the remaining 30 years of the asset's life giving a depreciation expense for the next year of ₹ 2,733 (₹ 82,000 / 30). The next year's finance cost for unwinding of discount will be ₹ 415 (₹ 8,300 × 5 per cent).

6.

At 31st March, 20X4:	₹
Asset at valuation (1)	1,26,600
Accumulated depreciation	Nil
Decommissioning liability	(11,600)
Net assets	1,15,000
Retained earnings (2)	(10,600)
Revaluation surplus (3)	15,600

Notes:

(1) When accounting for revalued assets to which decommissioning liabilities attach, it is important to understand the basis of the valuation obtained. For example:

(a) if an asset is valued on a discounted cash flow basis, some valuers may value the asset without deducting any allowance for decommissioning costs (a 'gross' valuation), whereas others may value the asset after deducting an allowance for decommissioning costs (a 'net' valuation), because an entity acquiring the asset will generally also assume the decommissioning obligation. For financial reporting purposes, the decommissioning obligation is recognized as a separate liability, and is not deducted from the asset. Accordingly, if the asset is valued on a net basis, it is necessary to adjust the valuation obtained by adding back the allowance for the liability, so that the liability is not counted twice.

(b) if an asset is valued on a depreciated replacement cost basis, the valuation obtained may not include an amount for the decommissioning component of the asset. If it does not, an appropriate amount will need to be added to the valuation to reflect the depreciated replacement cost of that component.

Since, the asset is valued on a net basis, it is necessary to adjust the valuation obtained by adding back the allowance for the liability. Valuation obtained of

© The Institute of Chartered Accountants of India

₹ 1,15,000 plus decommissioning costs of ₹ 11,600, allowed for in the valuation but recognized as a separate liability = ₹ 1,26,600.

(2) Three years' depreciation on original cost ₹ 1,20,000 × 3/40 = ₹ 9,000 plus cumulative discount on ₹ 10,000 at 5 per cent compound = ₹ 1,600; total ₹ 10,600.

(3) Revalued amount ₹ 1,26,600 less previous net book value of ₹ 1,11,000 (cost ₹ 120,000 less accumulated depreciation ₹ 9,000).

The depreciation expense for 20X4-20X5 is therefore ₹ 3,420 (₹ 1,26,600 x 1 / 37) and the discount expense for 20X5 is ₹ 600 (11,600 x 5% = 580 or 600 (to the nearest 100). On 31st March, 20X5, the decommissioning liability (before any adjustment) is ₹ 12,200. However, as per the estimate of the entity, the present value of the decommissioning liability has decreased by ₹ 5,000. Accordingly, the entity adjusts the decommissioning liability from ₹ 12,200 to ₹ 7,200.

The whole of this adjustment is taken to revaluation surplus, because it does not exceed the carrying amount that would have been recognized had the asset been carried under the cost model. If it had done, the excess would have been taken to profit or loss. The entity makes the following journal entry to reflect the change:

		₹	₹
Provision for decommissioning liability	Dr.	5,000	
To Revaluation surplus			5,000

As at 31st March, 20X5, the entity revalued its asset at ₹ 1,07,000, which is net of an allowance of ₹ 7,200 for the reduced decommissioning obligation that should be recognized as a separate liability. The valuation of the asset for financial reporting purposes, before deducting this allowance, is therefore ₹ 1,14,200. The following additional journal entry is needed:

Notes:

		₹	₹
Accumulated depreciation (1)	Dr.	3,420	
To Asset at valuation			3,420
Revaluation surplus (2)	Dr.	8,980	
To Asset at valuation (3)			8,980

(1) Eliminating accumulated depreciation of ₹ 3,420 in accordance with the entity's accounting policy.

© The Institute of Chartered Accountants of India

(2) The debit is to revaluation surplus because the deficit arising on the revaluation does not exceed the credit balance existing in the revaluation surplus in respect of the asset.

(3) Previous valuation (before allowance for decommissioning costs) ₹ 1,26,600, less cumulative depreciation ₹ 3,420, less new valuation (before allowance for decommissioning costs) ₹ 1,14,200.

Following this valuation, the amounts included in the balance sheet are:

Asset at valuation	1,14,200
Accumulated depreciation	Nil
Decommissioning liability	(7,200)
Net assets	1,07,000
Retained earnings (1)	(14,620)
Revaluation surplus (2)	11,620

Notes:

(1) ₹ 10,600 at 31st March, 20X4, plus depreciation expense of ₹ 3,420 and discount expense of ₹ 600 = ₹ 14,620.

(2) ₹ 15,600 at 31st March, 20X4, plus ₹ 5,000 arising on the decrease in the liability, less ₹ 8,980 deficit on revaluation = ₹ 11,620.

7. The annual depreciation charges prior to the change in useful life were

Buildings	₹ 1,50,00,000/15 =	₹ 10,00,000
Plant and machinery	₹ 1,00,00,000/10 =	₹ 10,00,000
Furniture and fixtures	₹ 35,00,000/7 =	₹ 5,00,000
Total =		₹ 25,00,000 (A)

The revised annual depreciation for the year ending 31st March, 20X5, would be

Buildings	[₹1,50,00,000 – (₹ 10,00,000 × 3)] / 10	₹ 12,00,000
Plant and machinery	[₹ 1,00,00,000 – (₹ 10,00,000 × 3)] / 7	₹ 10,00,000
Furniture and fixtures	[₹ 35,00,000 – (₹ 5,00,000 × 3)] / 5	₹ 4,00,000
Total		₹ 26,00,000 (B)

The impact on Statement of Profit and Loss for the year ending 31st March, 20X5

= ₹ 26,00,000 – ₹ 25,00,000 = ₹ 1,00,000

© The Institute of Chartered Accountants of India

This is a change in accounting estimate which is adjusted prospectively in the period in which the estimate is amended and, if relevant, to future periods if they are also affected. Accordingly, from 20X4-20X5 onward, excess of ₹ 1,00,000 will be charged in the Statement of Profit and Loss every year till the time there is any further revision.

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

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

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

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

9. According to paragraph 35 of Ind AS 16, when an item of property, plant and equipment is revalued, the carrying amount of that asset is adjusted to the revalued amount. At the date of the revaluation, the asset is treated in one of the following ways:

(a) The gross carrying amount is adjusted in a manner that is consistent with the revaluation of the carrying amount of the asset. For example, the gross carrying amount may be restated by reference to observable market data or it may be restated proportionately to the change in the carrying amount. The accumulated depreciation at the date of the revaluation is adjusted to equal the difference between the gross carrying amount and

© The Institute of Chartered Accountants of India

the carrying amount of the asset after taking into account accumulated impairment losses.

In such a situation, the revised carrying amount of the machinery will be as follows:

Gross carrying amount	₹ 250	[(200/120) x 150]
Net carrying amount	₹ 150	
Accumulated depreciation	₹ 100	(₹ 250 – ₹ 150)

Journal entry

Plant and Machinery (Gross Block)	Dr.	₹ 50	
To Accumulated Depreciation			₹ 20
To Revaluation Reserve			₹ 30

Depreciation subsequent to revaluation

Since the Gross Block has been restated, the depreciation charge will be ₹ 25 per annum (₹ 250/10 years).

Journal entry

Accumulated Depreciation	Dr.	₹ 25 p.a.	
To Plant and Machinery (Gross Block)			₹ 25 p.a.

(b) The accumulated depreciation is eliminated against the gross carrying amount of the asset.

The amount of the adjustment of accumulated depreciation forms part of the increase or decrease in carrying amount that is accounted for in accordance with the paragraphs 39 and 40 of Ind AS 16.

In this case, the gross carrying amount is restated to ₹ 150 to reflect the fair value and accumulated depreciation is set at zero.

Journal entry

Accumulated Depreciation	Dr.	₹ 80	
To Plant and Machinery (Gross Block)			₹ 80
Plant and Machinery (Gross Block)	Dr.	₹ 30	
To Revaluation Reserve			₹ 30

© The Institute of Chartered Accountants of India

Depreciation subsequent to revaluation

Since the revalued amount is the revised gross block, the useful life to be considered is the remaining useful life of the asset which results in the same depreciation charge of ₹ 25 per annum as per Option A (₹ 150 / 6 years).

Journal entry

Accumulated Depreciation	Dr.	₹ 25 p.a.	
To Plant and Machinery (Gross Block)			₹ 25 p.a.

10. To answer this question one must make a materiality judgement.

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

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

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

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

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

11. **In the books of Heaven Ltd.**

Machinery A/c

Date	Particulars	Amount	Date	Particulars	Amount
1.4.2X01	To Bank/ Vendor	30,00,000	31.3.2X02	By Depreciation (W.N.1)	2,50,000
			31.3.2X02	By Balance c/d	27,50,000
		30,00,000			30,00,000
1.4.2X02	To Balance b/d	27,50,000	31.3.2X03	By Depreciation	2,50,000
			31.3.2X03	By Balance c/d	25,00,000
		27,50,000			27,50,000
1.4.2X03	To Balance b/d	25,00,000	31.3. 2X04	By Depreciation	2,50,000

© The Institute of Chartered Accountants of India

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

© The Institute of Chartered Accountants of India

Working Notes:

1. Calculation of useful life of machinery on 1.4.2X01

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

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

= ₹ 2,50,000

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

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

2. Depreciation after upward revaluation as on 1.4.2X06

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

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

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

3. Depreciation after downward revaluation as on 1.4.2X08

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

Revised useful life 8 years

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

4. Amount transferred from revaluation reserve

Revaluation reserve on 1.4.2X06 (A)	₹ 1,75,000
Remaining useful life	7 years
Amount transferred every year (1,75,000 / 7)	₹ 25,000
Amount transferred in 2 years (25,000 x 2) (B)	₹ 50,000
Balance of revaluation reserve on 1.4.2X08 (A-B)	₹ 1,25,000

5. Amount of downward revaluation to be charged to Profit and Loss Account

Downward revaluation as on 1.4.2X08 (W.N.3)	₹ 2,06,250
Less: Adjusted from Revaluation reserve (W.N.4)	(₹ 1,25,000)
Amount transferred to Profit and Loss Account	₹ 81,250

© The Institute of Chartered Accountants of India

FOR SHORTCUT TO IND AS WISDOM: SCAN ME!

TEST YOUR KNOWLEDGE

Questions

1. Marine Transport Limited ordered 3 ships for its fleet on 1st April, 20X0. It pays a down payment of 25% of the contract value of each of the ship out of long-term borrowings from a scheduled bank. The delivery has to commence from the financial year 20X7. On 1st March, 20X2, the ship builder informs that it has commenced production of one ship. There is no progress on other 2 ships. Marine Transport Limited prepares its financial statements on financial year basis.

   Advise whether it is permissible for Marine Transport Limited to capitalise any borrowing costs for the financial year ended 31st March, 20X1 or 31st March, 20X2.

2. X Limited has a treasury department that arranges funds for all the requirements of the Company including funds for working capital and expansion programs. During the year ended 31st March, 20X2, the Company commenced the construction of a qualifying asset and incurred the following expenses:

Date	Amount (₹)
1st July, 20X1	2,50,000
1st December, 20X1	3,00,000

   The details of borrowings and interest thereon are as under:

Particulars	Average Balance (₹)	Interest (₹)
Long term loan @ 10%	10,00,000	1,00,000
Working capital loan	5,00,000	65,000
	15,00,000	1,65,000

   Compute the borrowing costs that need to be capitalised.

© The Institute of Chartered Accountants of India

3. An entity constructs a new head office building commencing on 1st September 20X1, which continues till 31st December 20X1. Directly attributable expenditure at the beginning of the month on this asset are ₹ 1,00,000 in September 20X1 and ₹ 2,50,000 in each of the months of October to December 20X1.

   The entity has not taken any specific borrowings to finance the construction of the asset but has incurred finance costs on its general borrowings during the construction period. During the year, the entity had issued 10% debentures with a face value of ₹ 20 lacs and had an overdraft of ₹ 5,00,000, which increased to ₹ 7,50,000 in December 20X1. Interest was paid on the overdraft at 15% until 1 October 20X1, then the rate was increased to 16%.

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

4. K Ltd. began construction of a new building at an estimated cost of ₹ 7 lakh on 1st April, 20X1. To finance construction of the building it obtained a specific loan of ₹ 2 lakh from a financial institution at an interest rate of 9% per annum.

   The company's other outstanding loans were:

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

   The expenditure incurred on the construction was:

April, 20X1	₹ 1,50,000
August, 20X1	₹ 2,00,000
October, 20X1	₹ 3,50,000
January, 20X2	₹ 1,00,000

   The construction of building was completed by 31st January, 20X2.

   Following the provisions of Ind AS 23 'Borrowing Costs', calculate the amount of interest to be capitalized and pass necessary journal entry for capitalizing the cost and borrowing cost in respect of the building as on 31st January, 20X2.

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

© The Institute of Chartered Accountants of India

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

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

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

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

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

Determine the amount of the borrowing costs which can be capitalized at the year end as per relevant Ind AS.

6. In a group with Parent Company "P" there are 3 subsidiaries with following business:

"A" – Real Estate Company

"B" – Construction Company

"C" – Finance Company

- Parent Company has no operating activities of its own but performs management functions for its subsidiaries.
- Financing activities and cash management in the group are coordinated centrally.
- Finance Company is a vehicle used by the group solely for raising finance.
- All entities in the group prepare Ind AS financial statements.

The following information is relevant for the current reporting period 20X1-20X2:

Real Estate Company

- Borrowings of ₹ 10,00,000 with an interest rate of 7% p.a.

© The Institute of Chartered Accountants of India

- Expenditures on qualifying assets during the period amounted to ₹ 15,40,000.
- All construction works were performed by Construction Company. Amounts invoiced to Real Estate Company included 10% profit margin.

Construction Company

- No borrowings during the period.
- Financed ₹ 10,00,000 of expenditures on qualifying assets using its own cash resources.

Finance Company

- Raised ₹ 20,00,000 at 7% p.a. externally and issued a loan to Parent Company for general corporate purposes at the rate of 8%.

Parent Company

- Used loan from Finance Company to acquire a new subsidiary.
- No qualifying assets apart from those in Real Estate Company and Construction Company.
- Parent Company did not issue any loans to other entities during the period.

Compute the amount of borrowing costs eligible for capitalisation in the financial statements of each of the four entities for the current reporting period 20X1-20X2.

7. Examine how will you capitalise the interest, when qualifying assets are funded by borrowings in the nature of bonds that are issued at discount.

   Y Ltd. issued at the start of year 1, 10% (interest paid annually and having maturity period of 4 years) bonds with a face value of ₹ 2,00,000 at a discount of 10% to finance a qualifying asset which is ready for intended use at the end of year 2.

   Compute the amount of borrowing costs to be capitalized if the company amortizes discount using Effective Interest Rate method by applying 13.39% p.a. of EIR.

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

© The Institute of Chartered Accountants of India

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

Answers

1. As per paragraph 5 of Ind AS 23, a qualifying asset is an asset that necessarily takes a substantial period of time to get ready for its intended use or sale.

As per paragraph 17 of Ind AS 23, an entity shall begin capitalising borrowing costs as part of the cost of a qualifying asset on the commencement date. The commencement date for capitalisation is the date when the entity first meets all of the following conditions:

(a) It incurs expenditures for the asset.

(b) It incurs borrowing costs.

(c) It undertakes activities that are necessary to prepare the asset for its intended use or sale.

The ship is a qualifying asset as it takes substantial period of time for its construction. Thus, the related borrowing costs should be capitalised.

Marine Transport Limited borrows funds and incurs expenditures in the form of down payment on 1st April, 20X0. Thus, condition (a) and (b) are met. However, condition (c) is met only on 1st March, 20X2, and that too only with respect to one ship. Thus, there is no capitalisation of borrowing costs during the financial year ended 31st March, 20X1. Even during the financial year ended 31st March, 20X2, borrowing costs relating to the 'one' ship whose construction had commenced from 1st March, 20X2 will be capitalised from 1st March, 20X2 to 31st March, 20X2. All other borrowing costs are expensed.

2. The capitalisation rate is calculated as below:

Total borrowing costs / Weighted average total borrowings: 1,65,000/15,00,000 = 11%.

Interest to be capitalised is calculated as under:

— On ₹ 2,50,000 @ 11% p.a. for 9 months = ₹ 20,625

— On ₹ 3,00,000 @ 11% p.a. for 4 months = ₹ 11,000

Total interest capitalised for the year ended 31st March 20X2 is ₹ 31,625

© The Institute of Chartered Accountants of India

3. Since the entity has only general borrowing hence first step will be to compute the capitalisation rate. The capitalisation rate of the general borrowings of the entity during the period of construction is calculated as follows:

Finance cost on ₹ 20 lacs 10% debentures during September – December 20X1	₹ 66,667
Interest @ 15% on overdraft of ₹ 5,00,000 in September 20X1	₹ 6,250
Interest @ 16% on overdraft of ₹ 5,00,000 in October and November 20X1	₹ 13,333
Interest @ 16% on overdraft of ₹ 7,50,000 in December 20X1	₹ 10,000
Total finance costs in September – December 20X1	₹ 96,250

Weighted average borrowings during period

$$= \frac{(20,00,000 \times 4) + (500,000 \times 3) + (750,000 \times 1)}{4} = ₹\ 25,62,500$$

Capitalisation rate = Total finance costs during the construction period / Weighted average borrowings during the construction period

= 96,250 / 25,62,500 = 3.756%

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

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

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

Date of incurrence of expenditure	***Amount spent***	***Financed through***	***Calculation***	***₹***
1st April, 20X1	1,50,000	Specific borrowing	1,50,000 x 9% x 10/12	11,250

© The Institute of Chartered Accountants of India

1st August, 20X1	2,00,000	Specific borrowing	50,000 x 9% x 10/12	3,750
		General borrowing	1,50,000x11.4375% x 6/12	8,578.125
1st October, 20X1	3,50,000	General borrowing	3,50,000x11.4375% x 4/12	13,343.75
1st January, 20X2	1,00,000	General borrowing	1,00,000x11.4375% x 1/12	953.125
				37,875

Note: Since construction of building started on 1st April, 20X1, it is presumed that all the later expenditures on construction of building had been incurred at the beginning of the respective month.

(iii) Total expenses to be capitalized for building

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

(iv) Journal Entry

Date	***Particulars***	₹	₹
31.1.20X2	Building account Dr.	8,37,875	
	To Bank account		8,00,0000
	To Interest payable (borrowing cost)		37,875
	(Being expenditure incurred on construction of building and borrowing cost thereon capitalized)		

Note: In the above journal entry, it is assumed that interest amount will be paid at the year end. Hence, entry for interest payable has been passed on 31.1.20X2.

© The Institute of Chartered Accountants of India

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

Date	*Particulars*		₹	₹
31.1.20X2	Building account	Dr.	8,37,875	
	To Bank account			8,37,875
	(Being expenditure incurred on construction of building and borrowing cost thereon capitalized)			

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

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

Analysis of expenditure:

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

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

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

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

© The Institute of Chartered Accountants of India

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

6. Following is the treatment as per Ind AS 23:

Finance Company

No expenditure on qualifying assets have been incurred, so Finance Company cannot capitalise anything.

Real Estate Company

Total interest costs in the financial statements of Real Estate Company is ₹ 70,000. Expenditures on qualifying assets exceed total borrowings, so the total amount of interest can be capitalised.

Construction Company

No interest expense has been incurred, so Construction Company cannot capitalise anything.

Consolidated financial statements of Parent Company:

Total general borrowings of the group: ₹ 10,00,000 + ₹ 20,00,000 = ₹ 30,00,000

Although Parent Company used proceeds from loan to acquire a subsidiary, this loan cannot be excluded from the pool of general borrowings.

Total interest expenditures for the group = ₹ 30,00,000 x 7% = ₹ 2,10,000

Total expenditures on qualifying assets for the group are added up. Profit margin charged by Construction Company to Real Estate Company is eliminated:

Real Estate Company – ₹ 15,40,000/1.1 = ₹ 14,00,000

Construction Co – ₹ 10,00,000

Total consolidated expenditures on qualifying assets:

₹ (14,00,000 + 10,00,000) = ₹ 24,00,000

Capitalisation rate = 7%

© The Institute of Chartered Accountants of India

Borrowing costs eligible for capitalisation = ₹ 24,00,000 x 7% = ₹ 1,68,000

Total interest expenditures of the group are higher than borrowing costs eligible for capitalisation calculated based on the actual expenditures incurred on the qualifying assets. Therefore, only ₹ 1,68,000 can be capitalised.

7. Capitalisation Method

As per the Standard, borrowing costs may include interest expense calculated using the effective interest method. Further, capitalisation of borrowing cost should cease where substantially all the activities necessary to prepare the qualifying asset for its intended use or sale are complete.

Thus, only that portion of the amortized discount should be capitalised as part of the cost of a qualifying asset which relates to the period during which acquisition, construction or production of the asset takes place.

Capitalisation of Interest

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

Quantum of Borrowing

The value of the bond to Y Ltd. is the transaction price ie ₹ 1,80,000 (2,00,000 – 20,000)

Therefore, Y Ltd will recognize the borrowing at ₹ 1,80,000.

Computation of the amount of Borrowing Cost to be Capitalised

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

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

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

© The Institute of Chartered Accountants of India

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

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

Accordingly, the treatment of Interest of ₹ 68.20 lakh occurred during the year 20X1-20X2 would be as follows:

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

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

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

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

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

© The Institute of Chartered Accountants of India

FOR SHORTCUT TO IND AS WISDOM: SCAN ME!

TEST YOUR KNOWLEDGE

Questions

1. Apex Ltd. is engaged in manufacturing of steel utensils. It owns a building for its headquarters. The building used to be fully occupied for internal use. However, recently the company has undertaken a massive downsizing exercise as a result of which 1/3rd of the building became vacant. This vacant portion has now been given for on lease for 6 years.

   Determine the CGU of the building.

2. ABC Ltd. has three cash-generating units: A, B and C, the carrying amounts of which as on 31st March, 20X1 are as follows: **(₹ in crore)**

Cash-generating units	Carrying amount	Remaining useful life
A	500	10
B	750	20
C	1,100	20

ABC Ltd. also has two corporate assets having a remaining useful life of 20 years.

		(₹ in crore)
Corporate asset	**Carrying amount**	**Remarks**
X	600	The carrying amount of X can be allocated on a reasonable basis (i.e., pro rata basis) to the individual cash-generating units.
Y	200	The carrying amount of Y cannot be allocated on a reasonable

© The Institute of Chartered Accountants of India

		basis to the individual cash-generating units.

Recoverable amount as on 31st March, 20X1 is as follows:

Cash-generating units	Recoverable amount (₹ in crore)
A	600
B	900
C	1,400
ABC Ltd.	3,200

Calculate the impairment loss, if any. Ignore decimals.

3. Parent acquires an 80% ownership interest in Subsidiary for ₹ 2,100 on 1st April, 20X1. At that date, Subsidiary's net identifiable assets have a fair value of ₹ 1,500. Parent chooses to measure the non-controlling interests as the proportionate interest of Subsidiary's net identifiable assets. The assets of Subsidiary together are the smallest group of assets that generate cash inflows that are largely independent of the cash inflows from other assets or groups of assets. Since other cash-generating units of Parent are expected to benefit from the synergies of the combination, the goodwill of ₹ 500 related to those synergies has been allocated to other cash-generating units within Parent. On 31st March, 20X2, Parent determines that the recoverable amount of cash-generating unit Subsidiary is ₹ 1,000. The carrying amount of the net assets of Subsidiary, excluding goodwill, is ₹ 1,350.

   Allocate the impairment loss on 31st March, 20X2.

4. A Ltd. purchased a machinery of ₹ 100 crore on 1st April, 20X1. The machinery has a useful life of 5 years. It has nil residual value. A Ltd. adopts straight line method of depreciation for depreciating the machinery. Following information has been provided as on 31st March, 20X2:

Financial year	Estimated future cash flows (₹ in crore)
20X2-20X3	15
20X3-20X4	30
20X4-20X5	40
20X5-20X6	10

   Discount rate applicable : 10%

   Fair value less costs to sell as on 31st March, 20X2 : ₹ 70 crore

   Calculate the impairment loss, if any.

5. Assuming in the above question, as on 31st March, 20X3, there is no change in the estimated future cash flows and discount rate. Fair value less costs to sell as on 31st March, 20X3 is ₹ 40 crore.

   Advise, how it should deal with under Ind AS 36.

© The Institute of Chartered Accountants of India

6. A Ltd. purchased an asset of ₹ 100 lakh on 1st April, 20X0. It has useful life of 4 years with no residual value. Recoverable amount of the asset is as follows:

As on	Recoverable amount
31st March, 20X1	₹ 60 lakh
31st March, 20X2	₹ 40 lakh
31st March, 20X3	₹ 28 lakh

Calculate the amount of impairment loss or its reversal, if any, on 31st March, 20X1, 31st March, 20X2 and 31st March, 20X3.

7. On 31st March, 20X1, XYZ Ltd. makes following estimate of cash flows for one of its asset located in USA:

Year	Cash flows
20X1-20X2	US $ 80
20X2-20X3	US $ 100
20X3-20X4	US $ 20

Following information has been provided:

Particulars	India	USA
Applicable discount rate	15%	10%

Exchange rates are as follows:

As on	Exchange rate
31st March, 20X1	₹ 45/US $
31st March, 20X2	₹ 48/US $
31st March, 20X3	₹ 51/US $
31st March, 20X4	₹ 55/US $

Calculate value in use as on 31st March, 20X1.

8. Cash flow is ₹ 100, ₹ 200 or ₹ 300 with probabilities of 10%, 60% and 30%, respectively. Calculate expected cash flows.

9. Cash flow of ₹ 1,000 may be received in one year, two years or three years with probabilities of 10%, 60% and 30%, respectively. Calculate expected cash flows assuming applicable discount rate of 5%, 5.25% and 5.5% in year 1, 2 and 3, respectively.

10. Calculate expected cash flows in each of the following cases:

    (a) the estimated amount falls somewhere between ₹ 50 and ₹ 250, but no amount in the range is more likely than any other amount.

© The Institute of Chartered Accountants of India

(b) the estimated amount falls somewhere between ₹ 50 and ₹ 250, and the most likely amount is ₹ 100. However, the probabilities attached to each amount are unknown.

(c) the estimated amount will be ₹ 50 (10 per cent probability), ₹ 250 (30 per cent probability), or ₹ 100 (60 per cent probability).

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

Machinery A was purchased on 1st April 20X3 for ₹ 10 lakhs and residual value is ₹ 50 thousand. Machinery B was purchased on 1st April, 20X5 for ₹ 5 lakhs with no residual value. The useful life of both Machine A and B is 10 years. The Company expects following cash flows in the next 5 years pertaining to Machinery A. The incremental borrowing rate of the company is 10%.

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

On 31st March, 20X8, the professional valuers estimated that the current market value of Machinery A is ₹ 7 lakhs. The valuation fee was ₹ 1 lakh. There is a need to dismantle the machinery before delivering it to the buyer. The dismantling cost is ₹ 1.50 lakhs. Specialised packaging costs would be ₹ 25 thousand and legal fees would be ₹ 75 thousand.

The Inventory has been valued in accordance with Ind AS 2. The recoverable value of CGU is ₹ 10 Lakh as on 31st March, 20X8. In the next year, the company has done the assessment of recoverability of the CGU and found that the value of such CGU is ₹ 11 Lakhs ie on 31st March, 20X9. The recoverable value of Machine A is ₹ 4,50,000 and combined Machine A and B is ₹ 7,60,000 as on 31st March, 20X9.

Required:

a) Compute the impairment loss on CGU and carrying value of each asset after charging impairment loss for the year ending 31st March, 20X8 by providing all the relevant working notes to arrive at such calculation.

© The Institute of Chartered Accountants of India

b) Compute the prospective depreciation for the year 20X8-20X9 on the above assets.

c) Compute the carrying value of CGU as at 31st March, 20X9.

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

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

Assume a tax rate of 30%.

Determine the value in use of the machine in accordance with Ind AS 36?

13. PQR Ltd. is the company which has performed well in the past but one of its major assets, an item of equipment, suffered a significant and unexpected deterioration in performance.

© The Institute of Chartered Accountants of India

Management expects to use the machine for a further four years after 31st March 20X6, but at a reduced level. The equipment will be scrapped after four years. The financial accountant for PQR Ltd. has produced a set of cash-flow projections for the equipment for the next four years, ranging from optimistic to pessimistic. CFO thought that the projections were too conservative, and he intended to use the highest figures each year. These were as follows:

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

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

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

14. On 1st January Year 1, Entity Q purchased a machine costing ₹ 2,40,000 with an estimated useful life of 20 years and an estimated zero residual value. Depreciation is computed on straight-line basis. The asset had been re-valued on 1st January Year 3 to ₹ 2,50,000, but with no change in useful life at that date. On 1st January Year 4 an impairment review showed the machine's recoverable amount to be ₹ 1,00,000 and its estimated remaining useful life to be 10 years.

    Calculate:

    a) The carrying amount of the machine on 31st December Year 2 and the revaluation surplus arising on 1 January Year 3.

    b) The carrying amount of the machine on 31st December Year 3 (immediately before the impairment).

    c) The impairment loss recognised in the year to 31st December Year 4 and its treatment thereon

    d) The depreciation charge in the year to 31st December Year 4.

© The Institute of Chartered Accountants of India

Note: During the course of utilization of machine, the company did not opt to transfer part of the revaluation surplus to retained earnings.

Answers

1. CGU of the building is Apex Ltd. as a whole as the primary purpose of the building is to serve as a corporate asset.

2. **Allocation of corporate assets**

The carrying amount of X is allocated to the carrying amount of each individual cash-generating unit. A weighted allocation basis is used because the estimated remaining useful life of A's cash-generating unit is 10 years, whereas the estimated remaining useful lives of B and C's cash-generating units are 20 years.

				(₹ in crore)
Particulars	**A**	**B**	**C**	**Total**
Carrying amount	500	750	1,100	2,350
Useful life	10 years	20 years	20 years	—
Weight based on useful life	1	2	2	—
Carrying amount (after assigning weight)	500	1,500	2,200	4,200
Pro-rata allocation of X	12%	36%	52%	100%
	(500/4,200)	(1,500/4,200)	(2,200/4,200)	
Allocation of carrying amount of X	72	216	312	600
Carrying amount (after allocation of X)	572	966	1,412	2,950

Calculation of impairment loss

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

(a) Impairment loss of each cash-generating units

			(₹ in crore)
Particulars	**A**	**B**	**C**
Carrying amount (after allocation of X)	572	966	1,412
Recoverable amount			
Impairment loss			
	600	900	1400
	-	66	12

© The Institute of Chartered Accountants of India

(b) Allocation of the impairment loss between cash-generating units and corporate asset X, on a pro rata basis, as follows

				(₹ in crore)
Allocation to	**B**		**C**	
X	15	(66 x 216/966)	3	(12 x 312/1,412)
Other assets in cash-generating units	51	(66 x 750/ 966)	9	(12 x 1,100/ 1,412)
Impairment loss	66		12	

Step II: Impairment losses for the larger cash-generating unit, i.e., ABC Ltd. as a whole

						(₹ in crore)
Particulars	**A**	**B**	**C**	**X**	**Y**	**ABC Ltd.**
Carrying amount	500	750	1,100	600	200	3,150
Impairment loss (Step I)	-	(51)	(9)	(18)	-	(78)
Carrying amount (after Step I)	500	699	1,091	582	200	3,072
Recoverable amount						3,200
Impairment loss for the 'larger' cash-generating unit					Nil	

3. Non-controlling interests is measured as the proportionate interest of Subsidiary's net identifiable assets, i.e., ₹ 300 (20% of ₹ 1,500). Goodwill is the difference between the aggregate of the consideration transferred and the amount of the non-controlling interests (₹ 2,100 + ₹ 300) and the net identifiable assets (₹ 1,500), i.e., ₹ 900.

Since, the assets of Subsidiary together are the smallest group of assets that generate cash inflows that are largely independent of the cash inflows from other assets or groups of assets, therefore, Subsidiary is a cash-generating unit. Since other cash-generating units of Parent are expected to benefit from the synergies of the combination, the goodwill of ₹ 500 related to those synergies has been allocated to other cash-generating units within Parent. Because the cash-generating unit comprising Subsidiary includes goodwill within its carrying amount, it should be tested for impairment annually, or more frequently if there is an indication that it may be impaired.

Testing Subsidiary (cash-generating unit) for impairment

Goodwill attributable to non-controlling interests is included in Subsidiary's recoverable amount of ₹ 1,000 but has not been recognised in Parent's consolidated financial statements. Therefore, the carrying amount of Subsidiary should be grossed up to include goodwill

© The Institute of Chartered Accountants of India

attributable to the non-controlling interests, before being compared with the recoverable amount of ₹ 1,000. Goodwill attributable to Parent's 80% interest in Subsidiary at the acquisition date is ₹ 400 after allocating ₹ 500 to other cash-generating units within Parent. Therefore, goodwill attributable to the 20% non-controlling interests in Subsidiary at the acquisition date is ₹ 100.

Testing subsidiary for impairment on 31st March, 20X2

On 31st March, 20X2	Goodwill of subsidiary (₹)	Net identifiable assets (₹)	Total (₹)
Carrying amount	400	1,350	1,750
Unrecognised non-controlling interests	100	-	100
Adjusted carrying amount	**500**	**1,350**	**1,850**
Recoverable amount			1,000
Impairment loss			**850**

Allocating the impairment loss

The impairment loss of ₹ 850 should be allocated to the assets in the unit by first reducing the carrying amount of goodwill.

Therefore, ₹ 500 of the ₹ 850 impairment loss for the unit is allocated to the goodwill. If the partially owned subsidiary is itself a cash-generating unit, the goodwill impairment loss should be allocated to the controlling and non-controlling interests on the same basis as that on which profit or loss is allocated. In this case, profit or loss is allocated on the basis of relative ownership interests. Because goodwill is recognised only to the extent of Parent's 80% ownership interest in Subsidiary, Parent recognises only 80% of that goodwill impairment loss (i.e., ₹ 400).

The remaining impairment loss of ₹ 350 is recognised by reducing the carrying amounts of Subsidiary's identifiable assets.

Allocation of the impairment loss for Subsidiary on 31st March, 20X2

On 31st March, 20X2	Goodwill of subsidiary (₹)	Net identifiable assets (₹)	Total (₹)
Carrying amount	400	1,350	1,750
Impairment loss	(400)	(350)	(750)
Carrying amount after impairment loss	**-**	**1,000**	**1,000**

© The Institute of Chartered Accountants of India

4. Value in use of the machinery as on 31st March, 20X2 can be calculated as follows:

Financial year	Estimated cash flows (₹ in crore)	Present value factor @ 10%	Present value
20X2-20X3	15	0.9091	13.64
20X3-20X4	30	0.8264	24.79
20X4-20X5	40	0.7513	30.05
20X5-20X6	10	0.6830	6.83
			75.31

The recoverable amount of the machinery is ₹ 75.31 crore (higher of value in use of ₹ 75.31 crore and fair value *less* costs to sell of ₹ 70 crore). The carrying of the machinery is ₹ 80 crore (after providing for one year depreciation @ ₹ 20 crore). Therefore, the impairment loss of ₹ 4.69 crore should be provided in the books. Further, the impaired carrying value of ` 75.31 crore will be depreciated, on a straight-line basis, over the remaining four years.

5. Value in use of the machinery as on March 31,20X3 can be calculated as follows:

Financial year	Estimated cash flows (₹ in crore)	Present value factor @ 10%	Present value
20X3-20X4	30	0.9091	27.27
20X4-20X5	40	0.8264	33.06
20X5-20X6	10	0.7513	7.51
			67.84

The recoverable amount of the machinery is ₹ 67.84 crore (higher of value in use of ₹ 67.84 crore and fair value *less* costs to sell of ₹ 40 crore). Carrying amount of the machinery at the end of the year 20X2 is ₹ 56.48 crore (after providing for two years depreciation (100 – 20 - 4.69) - 18.83).

However, as per paragraph 116 of Ind AS 36, an impairment loss is not reversed just because of the passage of time (sometimes called the 'unwinding' of the discount), even if the recoverable amount of the asset becomes higher than its carrying amount. Reason being, the underlying reasons for the original impairment have not been removed, and the service potential of the asset has not increased.

Therefore, the impairment loss of ₹ 4.69 crore should not be reversed.

6. As on 31st March, 20X1

Carrying amount of the asset (opening balance)	₹ 100 lakh
Depreciation (₹ 100 lakh /4 years)	₹ 25 lakh
Carrying amount of the asset (closing balance)	₹ 75 lakh

© The Institute of Chartered Accountants of India

Recoverable amount (given)	₹ 60 lakh

Therefore, an impairment loss of ₹ 15 lakh should be recognised as on 31st March, 20X1. Depreciation for subsequent years should be charged on the carrying amount of the asset (after providing for impairment loss), i.e., ₹ 60 lakh.

As on 31st March, 20X2

Carrying amount of the asset (opening balance)	₹ 60 lakh
Depreciation (₹ 60 lakh /3 years)	₹ 20 lakh
Carrying amount of the asset (closing balance)	₹ 40 lakh

Therefore, no impairment loss should be recognised as on 31st March, 20X2.

As on 31st March, 20X3

Carrying amount of the asset (opening balance)	₹ 40 lakh
Depreciation (₹ 40 lakh / 2 years)	₹ 20 lakh
Carrying amount of the asset (closing balance)	₹ 20 lakh
Recoverable amount (given)	₹ 28 lakh

Since, the recoverable amount of the asset exceeds the carrying amount of the asset by ₹ 8 lakh, impairment loss recognised earlier should be reversed. However, reversal of an impairment loss should not exceed the carrying amount that would have been determined (net of amortisation or depreciation) had no impairment loss been recognised for the asset in prior years.

Carrying amount as on 31st March, 20X3 had no impairment loss being recognised would have been ₹ 25 lakh. Therefore, the reversal of an impairment loss of ₹ 5 lakh should be done as on 31st March, 20X3.

7.

Year	Cash flows (US $)	Present value factor @ 10%	Discounted cash flows (US $)
20X1-20X2	80	0.9091	72.73
20X2-20X3	100	0.8264	82.64
20X3-20X4	20	0.7513	15.03
Total Discounted cash flows in US $			170.40
Exchange rate as on 31st March, 20X1, i.e., date of calculating value in use			₹45/US $
Value in use as on 31st March, 20X1			₹ 7,668

© The Institute of Chartered Accountants of India

8.

Cash flows	Probability	Expected cash flow
100	10%	10
200	60%	120
300	30%	90
Total		220

The expected cash flow is ₹ 220.

9.

Year	Cash flows	P.V.F.	Present value	Probability	Expected cash flows
1	1,000	0.95238	952.38	10%	95.24
2	1,000	0.90273	902.73	60%	541.64
3	1,000	0.85161	851.61	30%	255.48
Total					892.36

The expected present value is ₹ 892.36.

10. (a) the estimated expected cash flow is ₹ 150 [(50 + 250)/2].

(b) the estimated expected cash flow is ₹ 133.33 [(50 + 100 + 250)/3].

(c) the estimated expected cash flow is ₹ 140 [(50 × 0.10) + (250 × 0.30) + (100 × 0.60)].

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

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

Machinery A		
Cost	(A)	₹ 10,00,000
Residual Value		₹ 50,000
Useful life		10 years
Useful life already elapsed		5 years
Yearly depreciation	(B)	₹ 95,000
WDV as at 31st March, 20X8 [A- (B x 5)]		**₹ 5,25,000**
Machinery B		
Cost	(C)	₹ 5,00,000
Residual Value		-
Useful life		10 years
Useful life already elapsed		3 years

© The Institute of Chartered Accountants of India

Yearly depreciation	(D)	₹ 50,000
WDV as at 31st March, 20X8 [C- (D x 3)]		**₹ 3,50,000**

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

Period	Cash Flows (₹)	PVF	PV
1	1,50,000	0.909	1,36,350
2	1,00,000	0.826	82,600
3	1,00,000	0.751	75,100
4	1,50,000	0.683	1,02,450
5	1,00,000	0.621	62,100
5	50,000	0.621	31,050
Value in use			**4,89,650**

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

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

(iv) Calculation of Impairment loss on Machinery A

	₹
Carrying Value	5,25,000
Less: Recoverable Value ie higher of Value-in-use and Fair value less cost of disposal	4,89,650
Impairment Loss	**35,350**

(v) Calculation of Impairment loss of CGU

1. First goodwill will be impaired fully and then the remaining impairment loss of ₹ 75,000 will be allocated to Machinery A and B.

2. If we allocate remaining impairment loss to Machinery A and B on pro-rata basis, it would come to ₹ 45,000 on Machinery A. However, the impairment loss of Machinery A cannot exceed ₹ 35,350. Hence, impairment to CGU will be as follows:

© The Institute of Chartered Accountants of India

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

* Balancing figure.

(b) Carrying value after adjustment of depreciation

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

(c) Calculation of carrying value of CGU as on 31st March, 20X9

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

Accordingly, the carrying value as on 31st March, 20X9 assuming that the impairment loss had never incurred, will be:

	Carrying Value	Recoverable Value	Final CV as at 31st Mar 20X9
Machinery A	4,30,000	4,50,000	4,30,000
Machinery B	3,00,000	(7,60,000 – 4,50,000) 3,10,000	3,00,000
Inventory	2,00,000	2,00,000	2,00,000
Goodwill	-		
Total	**9,30,000**	**9,60,000**	**9,30,000**

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

Note: It is assumed that value of inventory is same in 20X9 as it was in 20X8.

© The Institute of Chartered Accountants of India

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

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

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

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

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

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

Year ended	20X3-20X4	20X4-20X5	20X5-20X6	20X6-20X7	20X7-20X8	Value in use
Quantity (A)	10,000	10,500	11,025	11,576	12,155	
Price per unit (B)	₹ 200	₹ 206	₹ 212	₹ 219	₹ 225	
Estimated cash inflows (C=A x B)	₹ 20,00,000	₹ 21,63,000	₹ 23,37,300	₹ 25,35,144	₹ 27,34,875	
Misc. cash inflow disposal proceeds (D)					₹ 80 000	
Total estimated cash inflows (E=C+D)	₹ 20,00,000	₹ 21,63,000	₹ 23,37,300	₹ 25,35,144	₹ 28,14,875	
Cost per unit (F)	₹ 160	₹ 162	₹ 165	₹ 168	₹ 171	
Estimated cash outflows	(₹16,00,000)	(₹17,01,000)	(₹18,19,125)	(₹19,44,768)	(₹20,78,505)	

© The Institute of Chartered Accountants of India

(G = A x F)						
Misc. cash outflow: maintenance costs (H)			(₹ 50,000)			
Total estimated cash outflows (I=G+H)	(₹16,00,000)	(₹17,01,000)	(₹18,69,125)	(₹19,44,768)	(₹20,78,505)	
Net cash flows (J=E-I)	₹ 4,00,000	₹ 4,62,000	₹ 4,68,175	₹ 5,90,376	₹ 7,36,370	
Discount factor 8%* (K)	0.9259	0.8573	0.7938	0.7350	0.6806	
Discounted future cash flows (L=J x K)	₹ 3,70,360	₹ 3,96,073	₹ 3,71,637	₹ 4,33,926	₹ 5,01,173	₹20,73,169

* Since the future cash flows are estimated on a pre-tax basis, the discount rate is also determined on a pre-tax basis.

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

Calculation of Value in Use:

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

Calculation of Recoverable amount:

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

Calculation of Impairment loss:

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

© The Institute of Chartered Accountants of India

Calculation of Revised carrying amount:

Particulars	Amount (₹)
Carrying amount	6,60,000
Less: Impairment loss	(71,770)
Revised carrying amount	5,88,230

Calculation of Revised Depreciation:

Revised carrying amount – Residual value

Remaining life = (5,88,230 - 0) / 4 = ₹ 1,47,058 per annum

Set off of Impairment loss:

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

Treatment of Government compensation:

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

14. (a) Calculation of Carrying amount of machine at the end of Year 2

	₹
Cost of machine	2,40,000
Accumulated depreciation for 2 years [2 years × (2,40,000 ÷ 20)]	(24,000)
Carrying amount of the machine at the end of Year 2	2,16,000

(b) Calculation of carrying amount of the machine on 31 December Year 3

	₹
Carrying amount at the beginning of Year 3	2,16,000
Revaluation done at the beginning of Year 3	2,50,000
Revaluation surplus	34,000

(c) Calculation of Impairment loss at the end of Year 4

When machine is revalued on 1 January Year 3, depreciation is charged on the revalued amount over its remaining expected useful life.

Valuation at 1 January (re-valued amount)	2,50,000
Accumulated depreciation in Year 3 (2,50,000 / 18)	(13,889)
Carrying amount of the asset at the end of Year 3	2,36,111
On 1 January Year 4, recoverable amount of the machine	1,00,000

© The Institute of Chartered Accountants of India

Impairment loss (2,36,111 – 1,00,000)	1,36,111

An impairment loss of ₹ 34,000 will be taken to other comprehensive income (reducing the revaluation surplus for the asset to zero)

The remaining impairment loss of ₹ 1,02,111 (1,36,111 – 34,000) is recognised in the Statement of Profit and Loss for the Year 4.

(d) Calculation of depreciation charge in the Year 4

Carrying value of the machine at the beginning of Year 4	₹ 1,00,000
Estimated remaining useful life	10 years
Depreciation charge is (₹ 1,00,000 / 10 years)	₹ 10,000

© The Institute of Chartered Accountants of India

FOR SHORTCUT TO IND AS WISDOM: SCAN ME!

TEST YOUR KNOWLEDGE

Questions

1. X Ltd. is engaged in the business of publishing Journals. They acquired 100% stake in Y Ltd., a company in the same industry. X Ltd. paid purchase consideration of ₹ 10,00,00,000 and fair value of net assets acquired is ₹ 8,50,00,000. The purchase consideration includes payment for the following as well:

   (a) ₹ 30,00,000 for obtaining the skilled staff of Y Ltd.

   (b) ₹ 50,00,000 by way of payment towards 'Non-compete Fee' so as to restrict Y Ltd. to compete in the same line of business for next 5 years.

   However, the above items (a) and (b) are not forming part of the net assets acquired of ₹ 8,50,00,000.

   Determine how the above transactions be accounted for by X Ltd.

2. X Ltd. purchased a franchise from a restaurant chain at a cost of ₹ 1,00,00,000 and the franchise has 10 years life. In addition, the franchise agreement mentions that the franchisee would also pay the franchisor royalty as a percentage of sales made.

   Advise whether the franchise rights be treated as an intangible asset under Ind AS 38.

3. An entity regularly places advertisements in newspapers advertising its products and includes a reply slip that informs individuals replying to the advertisement that the entity may pass on the individual's details to other sellers of similar products, unless the individual ticks a box in the advertisement.

© The Institute of Chartered Accountants of India

Over a period of time the entity has assembled a list of customers' names and addresses. The list is provided to other entities for a fee. The entity would like to recognize an asset in respect of the expected future economic benefits to be derived from the list.

Evaluate whether the customer list be treated as an intangible asset under Ind AS 38.

4. A software company X Ltd. is developing new software for the telecom industry. It employs 100 employs engineers trained in that particular discipline who are engaged in the development of the software. X Ltd. feels that it has an excellent HR policy and does not expect any of its employees to leave in the near future. It wants to recognize these set of engineers as a human resources asset in the form of an intangible asset.

   Advise X Ltd. on the above issue.

5. X Ltd. has acquired a telecom license from Government to operate mobile telephony in two states of India.

   Recommend the cost of acquisition to be capitalised as an intangible asset under Ind AS 38.

6. X Ltd. purchased a standardised finance software at a list price of ₹ 30,00,000 and paid ₹ 50,000 towards purchase tax which is non-refundable. In addition to this, the entity was granted a trade discount of 5% on the initial list price. X Ltd. incurred cost of ₹ 7,00,000 towards customisation of the software for its intended use. X Ltd. also purchased a 5-year maintenance contract with the vendor company of ₹ 2,00,000.

   Identify at what cost the intangible asset will be recognized.

7. X Limited in a business combination, purchased the net assets of Y Limited for ₹ 4,00,000 on 31st March, 20X1. The assets and liabilities position of Y Limited just before the acquisition is as follows:

Assets	**Cost (in ₹)**
Property, Plant & Equipment	1,00,000
Intangible asset 1	20,000
Intangible asset 2	50,000
Cash & Bank	1,30,000
Liabilities	
Trade payable	50,000

The fair market value of the PPE, intangible asset 1 and intangible asset 2 is available and they are ₹ 1,50,000, ₹ 30,000 and ₹ 70,000 respectively.

Recommend how would X Limited account for the net assets acquired from Y Limited.

© The Institute of Chartered Accountants of India

8. X Ltd. acquired Y Ltd. on 30th April, 20X1. The purchase consideration is ₹ 50,00,000. The fair value of the tangible assets is ₹ 45,00,000. The company estimates the fair value of "in-process research and development projects" at ₹ 10,00,000. No other Intangible asset is acquired by X Ltd. in the transaction. Further, cost incurred by X Ltd. in relation to that research and development project is as follows:

   (a) ₹ 5,00,000 – as research expenses

   (b) ₹ 2,00,000 – to establish technological feasibility

   (c) ₹ 7,00,000 – for further development cost after technological feasibility is established.

   Determine at what amount the intangible asset be measured under Ind AS 38.

9. X Ltd. acquired a patent right of manufacturing drug from Y Ltd. In exchange X Ltd. gives its intellectual property right to Y Ltd. Current market value of the patent and intellectual property rights are ₹ 20,00,000 and ₹ 18,00,000 respectively.

   Compute the value of patent right for initial recognition in the books of X Ltd. in following two situations:

   (a) X Ltd. did not pay any cash to Y Ltd.

   (b) X Ltd. pays ₹ 2,00,000 to Y Ltd.

10. X Garments Ltd. spent ₹ 1,00,00,000 towards promotions for a fashion show by way of various on-road shows, contests etc.

    After that event, it realised that the brand name of the entity got popular and resultantly, subsequent sales have shown a significant improvement. It is further expected that this hike will have an effect over the next 2-3 years.

    Advise how the entity should account for the above cost incurred on promoting such show.

11. An entity is developing a new production process. During 20X1-20X2, expenditure incurred was ₹ 1,000, of which ₹ 900 was incurred before 1st March, 20X2 and ₹ 100 was incurred between 1st March, 20X2 and 31st March, 20X2. The entity is able to demonstrate that at 1st March, 20X2, the production process met the criteria for recognition as an intangible asset. The recoverable amount of the know-how embodied in the process (including future cash outflows to complete the process before it is available for use) is estimated to be ₹ 500.

    During 20X2-20X3, expenditure incurred is ₹ 2,000. At the end of 20X3, the recoverable amount of the know-how embodied in the process (including future cash outflows to complete the process before it is available for use) is estimated to be ₹ 1,900.

© The Institute of Chartered Accountants of India

Tabulate the accounting treatment of expenditure incurred in 20X1-20X2 and 20X2-20X3 as per relevant Ind AS. Ignore effects of amortisation.

12. X Ltd. is engaged in developing computer software. The expenditures incurred by X Ltd. in pursuance of its development of software is given below:

    (a) Paid ₹ 2,00,000 towards salaries of the program designers.

    (b) Incurred ₹ 5,00,000 towards other cost of completion of program design.

    (c) Incurred ₹ 2,00,000 towards cost of coding and establishing technical feasibility.

    (d) Paid ₹ 7,00,000 for other direct cost after establishment of technical feasibility.

    (e) Incurred ₹ 2,00,000 towards other testing costs.

    (f) A focus group of other software developers was invited to a conference for the introduction of this new software. Cost of the conference aggregated to ₹ 70,000.

    On 15th March, 20X1, the development phase was complete, and a cash flow budget was prepared. Net profit for the year was estimated to be equal ₹ 40,00,000.

    Interpret how X Ltd. should account for the above-mentioned cost.

13. X Ltd. has started developing a new production process in financial year 20X1-20X2. Total expenditure incurred till 30th September, 20X1, was ₹ 1,00,00,000. The expenditure on the development of the production process meets the recognition criteria on 1st July, 20X1. The records of X Ltd. show that, out of total ₹ 1,00,00,000, ₹ 70,00,000 were incurred during July to September, 20X1. X Ltd. publishes its financial results quarterly.

    Determine how X Ltd. should account for the development expenditure.

14. X Ltd. decides to revalue its intangible assets on 1st April, 20X1. On the date of revaluation, the intangible assets stand at a cost of ₹ 1,00,00,000 and accumulated amortisation is ₹ 40,00,000. The intangible assets are revalued at ₹ 1,50,00,000.

    Analyse how should X Ltd. account for the revalued intangible assets in its books of account.

15. One of the senior engineers at XYZ has been working on a process to improve manufacturing efficiency and, consequently, reduce manufacturing costs. This is a major project and has the full support of XYZ's board of directors. The senior engineer believes that the cost reductions will exceed the project costs within twenty-four months of their implementation. Regulatory testing and health and safety approval was obtained on 1st June 20X5. This removed uncertainties concerning the project, which was finally completed on 20th April 20X6. Costs of ₹ 18,00,000, incurred during the year till 31st March 20X6, have been recognized as an intangible asset. An offer of ₹ 7,80,000 for the new developed technology has been

© The Institute of Chartered Accountants of India

received by potential buyer but it has been rejected by XYZ. Utkarsh believes that the project will be a major success and has the potential to save the company ₹ 12,00,000 in perpetuity. Director of research at XYZ, Neha, who is a qualified electronic engineer, is seriously concerned about the long-term prospects of the new process and she is of the opinion that competitors would have developed new technology at some time which would require to replace the new process within four years. She estimates that the present value of future cost savings will be ₹ 9,60,000 over this period. After that, she thinks that there is no certainty about its future.

Advise the appropriate accounting treatment for the aforesaid issue for the year ended 31st March, 20X6.

Answers

1. X Ltd. should recognize an intangible asset in respect of the consideration paid towards 'Non-Compete Fee'.

However, amount paid for obtaining skilled staff amounting to ₹ 30,00,000 does not meet the definition of intangible asset since X Ltd. has not established any right over the resource and the same should be expensed. The entity has insufficient control over the expected future economic benefits arising from the team of skilled staff.

Therefore, ₹ 50,00,000 will be separately recognized as an intangible asset, whereas amount paid for obtaining skilled staff does not meet the recognition criteria for being identified as a separate intangible asset. However, since it is acquired as part of a business combination, it forms part of the goodwill recognized at the acquisition date.

The value of goodwill would be ₹ 1,00,00,000 (₹ 1,50,00,000 – ₹ 50,00,000).

2. The franchise rights meets the identification criterion of an intangible asset since it arises from the contractual rights. It is acquired separately and it's cost can be measured reliably. In addition, X Ltd. will have future economic benefits and control over them from the franchise rights.

X Ltd. should recognize the franchise right as intangible asset and amortise it over 10 years. Royalty as a percentage of sales paid to the franchisor would be a charge to the profit and loss in the books of the X Ltd.

3. In this situation, the entity has no legal rights to the customer relationship, but exchange transactions have taken place that evidence separability of the asset and the control that the entity is able to exercise over the asset. Therefore, the list is an intangible asset. However, the entity may not recognize the asset because the cost of generating the customer list internally cannot be distinguished from the cost of developing the business as

© The Institute of Chartered Accountants of India

a whole. It does not meet the conditions specified to recognize an internally generated intangible asset.

4. Although, without doubt the skill sets of the employees make them extremely valuable to the company, however it does not have control over them. Merely having good HR policies would not make them eligible to be recognized as an intangible asset.

5. Cost of acquisition of the telecom license can be capitalised as an intangible asset under the head Licenses, as the cost is ascertainable, and it will lead to future economic benefits for X Ltd.

6. In accordance with Ind AS 38, the cost of a separately acquired intangible asset is its purchases price and non-refundable purchase taxes, after deducting trade discounts and rebates and any directly attributable cost of preparing the asset for its intended use.

Therefore, the initial cost of the asset should be:

	Amount (₹)
List price	30,00,000
Less: Trade discount (5%)	(1,50,000)
	28,50,000
Non-refundable purchase tax	50,000
Customisation cost	7,00,000
Total cost	36,00,000

The maintenance contract of ₹ 2,00,000 is an expense and therefore should be taken as a prepaid expense and charged to profit and loss over a period of 5 years.

7. X Limited will account for the assets acquired from Y Limited in following manner:

Assets	**Amount (₹)**
Property, plant and equipment	1,50,000
Goodwill	70,000
Intangible asset 1	30,000
Intangible asset 2	70,000
Cash & Bank	1,30,000
Liabilities	
Trade payable	50,000

© The Institute of Chartered Accountants of India

Note 1- Goodwill is the difference between fair value of net assets acquired and purchase consideration paid when is calculated as follow:

Goodwill = ₹ 4,00,000 – ₹ (1,50,000 + 70,000 + 30,000 + 1,30,000 – 50,000) = ₹ 70,000.

8. X Ltd. should initially recognize the acquired "in house research and development project" at its fair value i.e., ₹ 10,00,000. Research cost of ₹ 5,00,000 and cost of ₹ 2,00,000 for establishing technical feasibility should be charged to profit & loss. Costs incurred from the point of technological feasibility/asset recognition criteria until the time when development costs are incurred are capitalised. So the intangible asset should be recognized at ₹ 17,00,000 (₹ 10,00,000 + ₹ 7,00,000).

9. If an entity is able to determine reliably the fair value of either the asset received or the asset given up, then the fair value of the asset given up is used to measure cost unless the fair value of the asset received is more clearly evident.

The transaction at the fair value of the asset received adjusted for any cash received or paid. Therefore, in case (a) patent is measured at ₹ 18,00,000, in case (b) it is measured at ₹ 20,00,000 (18,00,000 + 2,00,000).

10. Expenditure of ₹ 1,00,00,000 though increased future economic benefits, but it does not result in creation of an intangible asset.

Such promotional cost should be expensed off.

11. At the end of the financial year 20X2, the production process is recognized as an intangible asset at a cost of ₹ 100 (expenditure incurred since the date when the recognition criteria were met, i.e., 1st March, 20X2). ₹ 900 expenditure incurred before 1st March, 20X2 is recognized as an expense because the recognition criteria were not met until 1st March, 20X2. This expenditure does not form part of the cost of the production process recognized in the balance sheet.

At the end of 20X3, the cost of the production process is ₹ 2,100 (₹ 100 expenditure recognized at the end of 20X2 plus ₹ 2,000 expenditure recognized in 20X3). The entity recognizes an impairment loss of ₹ 200 to adjust the carrying amount of the process before impairment loss (₹ 2,100) to its recoverable amount (₹ 1,900). This impairment loss will be reversed in a subsequent period if the requirements for the reversal of an impairment loss in Ind AS 36 are met.

12. Costs incurred in creating computer software, should be charged to research & development expenses when incurred until technical feasibility/asset recognition criteria have been established for the product. Here, technical feasibility is established after completion of detailed program design.

© The Institute of Chartered Accountants of India

In this case, ₹ 9,00,000 (salary cost of ₹ 2,00,000, program design cost of ₹ 5,00,000 and coding and technical feasibility cost of ₹ 2,00,000) would be recorded as expense in Profit and Loss since it belongs to research phase.

Cost incurred from the point of technical feasibility are capitalised as software costs. But the conference cost of ₹ 70,000 would be expensed off.

In this situation, direct cost after establishment of technical feasibility of ₹ 7,00,000 and testing cost of ₹ 2,00,000 will be capitalised.

The cost of software capitalised is = ₹ (7,00,000 + 2,00,000) = ₹ 9,00,000.

13. X Ltd. should recognize the intangible asset at ₹ 70,00,000 and ₹ 30,00,000 which was already recognized as an expense in first quarter should not be capitalised.

14. The intangible assets are revalued to ₹ 1,50,00,000 on an amortised replacement cost basis, which is a 2.5 times increase from its net value. Thereby applying the existing ratio of accumulated depreciation to the cost the revalued gross amount would be ₹ 2,50,00,000 gross and ₹ 1,00,00,000 on amortisation.

Alternatively, the net block can be increased by ₹ 90,00,000.

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

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

Since the project was completed on 20th April, 20X6, on 31st March, 20X6, the amount of ₹ 15,00,000 (₹ 18,00,000 x 10/12) should be capitalised in the balance sheet of year ending 20X5-20X6 representing expenditure since 1st June 20X5.

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

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

© The Institute of Chartered Accountants of India

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

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

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

Calculation of Impairment loss of intangible asset under development:

Particulars	₹
Carrying amount	15,00,000
Less: Recoverable amount	9,60,000
Impairment loss	5,40,000

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

Necessary adjusting entry to correct books of account will be:

		₹	₹
Operating expenses- Development expenditure	Dr.	3,00,000	
Operating expenses–Impairment loss	Dr.	5,40,000	
To Intangible asset under development			8,40,000

© The Institute of Chartered Accountants of India

FOR SHORTCUT TO IND AS WISDOM: SCAN ME!

TEST YOUR KNOWLEDGE

Questions

1. On 1st April, 20X1 an entity acquired an investment property (building) for ₹ 40,00,000. Management estimates the useful life of the building as 20 years measured from the date of acquisition. The residual value of the building is ₹ 2,00,000. Management believes that the straight-line depreciation method reflects the pattern in which it expects to consume the building's future economic benefits. What is the carrying amount of the building on 31st March, 20X2?

2. X Limited has an investment property (building) which is carried in Balance Sheet on 31st March, 20X1 at ₹ 15,00,000. During the year X Limited has stopped letting out the building and used it as its office premise. On 31st March, 20X1, management estimates the recoverable amount of the building as ₹ 10,00,000 and its remaining useful life as 20 years and residual value is nil. How should X Limited account for the above investment property as on 31st March, 20X1?

3. In financial year 20X1-20X2, X Limited incurred the following expenditure in acquiring property consisting of 6 identical houses each with separate legal title including the land on which it is built.

   The expenditure incurred on various dates is given below:

   On 1st April, 20X1 - Purchase cost of the property ₹ 1,80,00,000.

   On 1st April, 20X1 – Non-refundable transfer taxes ₹ 20,00,000 (not included in the purchase cost).

© The Institute of Chartered Accountants of India

On 2nd April, 20X1- Legal cost related to property acquisition ₹ 5,00,000.

On 6th April, 20X1- Advertisement campaign to attract tenants ₹ 3,00,000.

On 8th April, 20X1 - Opening ceremony function for starting business ₹ 1,50,000.

Throughout 20X1-20X2, incurred ₹ 1,00,000 towards day-to-day repair maintenance and other administrative expenses.

X Limited uses one of the six houses for office and accommodation of its few staffs. The other five houses are rented to various independent third parties.

How X Limited will account for all the above-mentioned expenses in the books of account?

4. X Ltd. is engaged in the construction industry and prepares its financial statements up to 31st March each year. On 1st April, 20X1, X Ltd. purchased a large property (consisting of land) for ₹ 2,00,00,000 and immediately began to lease the property to Y Ltd. on an operating lease. Annual rentals were ₹ 20,00,000. On 31st March, 20X5, the fair value of the property was ₹ 2,60,00,000. Under the terms of the lease, Y Ltd. was able to cancel the lease by giving six months' notice in writing to X Ltd. Y Ltd. gave this notice on 31st March, 20X5 and vacated the property on 30th September, 20X5. On 30th September, 20X5, the fair value of the property was ₹ 2,90,00,000. On 1st October, 20X5, X Ltd. immediately began to convert the property into ten separate flats of equal size which X Ltd. intended to sell in the ordinary course of its business. X Ltd. spent a total of ₹ 60,00,000 on this conversion project between 30th September, 20X5 to 31st March, 20X6. The project was incomplete at 31st March, 20X6 and the directors of X Ltd. estimate that they need to spend a further ₹ 40,00,000 to complete the project, after which each flat could be sold for ₹ 50,00,000.

   Examine and show how the three events would be reported in the financial statements of X Ltd. for the year ended 31st March, 20X6 as per Ind AS.

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

   Following information is relevant for Building A for the year ending 31st March, 20X2:

   Building A was initially purchased at the cost of ₹ 10 crores. At that time, the useful life of the building was estimated to be 20 years; out of which 5 years have been expired as on 1st April, 20X1. The company follows straight line method for depreciation.

   During the year, the company has invested in another Building B with the purpose to hold it for capital appreciation. The property was purchased on 1st April, 20X1 at the cost of

© The Institute of Chartered Accountants of India

₹ 2 crores. Expected life of the building is 40 years. As usual, the company follows straight line method of depreciation.

Further, during the year 20X1-20X2 the company earned/incurred following direct operating expenditure relating to Building A and Building B:

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

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

The other key inputs for valuation are as follows:

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

Assume that the fair value of properties based on discounted cash flow method is measured at ₹ 10.50 crores. The treatment of fair value of properties is to be given in the financials as per the requirements of Indian accounting standards.

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

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

© The Institute of Chartered Accountants of India

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

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

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

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

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

Answers

1. Cost of the asset is ₹ 40,00,000.

Depreciable amount = Cost less Residual value = ₹ (40,00,000 - 2,00,000) = ₹ 38,00,000

Depreciation for the year = Depreciable amount/useful life

= ₹ 38,00,000/20

= ₹ 1,90,000.

Carrying amount = Cost less accumulated depreciation

= ₹ (40,00,000 - 1,90,000) = ₹ 38,10,000.

2. At 31st March, 20X1, X Limited must transfer the property from investment property to property, plant and equipment since there is a change in use of the said building.

The transfer should be made at its carrying amount i.e., ₹ 15,00,000.

Since recoverable amount of the property as on 31st March, 20X1 is ₹ 10,00,000, impairment loss ₹ 5,00,000 should be recognized in the Statement of Profit and Loss. So, the carrying amount of Investment property at 31st March, 20X1 would be ₹ 10,00,000.

The entity must disclose the reclassification.

From April, 20X1, X Limited will depreciate the building over its remaining useful life of 20 years.

© The Institute of Chartered Accountants of India

3. The cost of the property = ₹ (1,80,00,000 + 20,00,000 + 5,00,000) = ₹ 2,05,00,000.

Since five houses out of six are being rented, so 5/6th of the property cost will be accounted for as an investment property and 1/6th of the property cost will be accounted for as owner-occupied property.

Cost of the investment property = ₹ 2,05,00,000 x 5/6 = ₹ 1,70,83,333

Cost of the owner-occupied property = ₹ (2,05,00,000 - 1,70,83,333) = ₹ 34,16,667.

All other costs, i.e., advertisement expenses, ceremony expenses and repair maintenance expenses will be expensed off as and when incurred.

4. From 1st April, 20X1, the property would be regarded as an investment property since it is being held for its investment potential rather than being owner occupied or developed for sale.

The property would be measured under the cost model. This means it will be measured at ₹ 2,00,00,000 at each year end.

On 30th September, 20X5, the property ceases to be an investment property. X Ltd. begins to develop it for sale as flats.

As per para 59 of Ind AS 40, transfers between investment property, owner-occupied property and inventories do not change the carrying amount of the property transferred and they do not change the cost of that property for measurement or disclosure purposes. Hence, the carrying value of the reclassified property will be ₹ 2,00,00,000.

Since the lease of the property is an operating lease, rental income of ₹ 10,00,000 (₹ 20,00,000 x 6/12) would be recognized in P/L for the year ended 31st March, 20X6.

The additional costs of ₹ 60,00,000 for developing the flats which were incurred up to and including 31st March, 20X6 would be added to the 'cost' of inventory to give a closing cost of ₹ 2,60,00,000.

The total selling price of the flats is expected to be ₹ 5,00,00,000 (10 x ₹ 50,00,000). Since the further costs to develop the flats total ₹ 40,00,000, their net realisable value is ₹ 4,60,00,000 (₹ 5,00,00,000 – ₹ 40,00,000), so the flats will be measured at a cost of ₹ 2,60,00,000.

The flats will be shown in inventory as a current asset.

5. Investment property is held to earn rentals or for capital appreciation or both. Ind AS 40 shall be applied in the recognition, measurement and disclosure of investment property. An investment property shall be measured initially at its cost. After initial recognition, an entity

© The Institute of Chartered Accountants of India

shall measure all of its investment properties in accordance with Ind AS 16's requirements for cost model.

The measurement and disclosure of Investment property as per Ind AS 40 in the balance sheet would be depicted as follows:

INVESTMENT PROPERTIES:	
Particulars	**Period ended 31st March, 20X2 (₹ in crores)**
Gross Amount:	
Opening balance (A)	10.00
Additions during the year (B)	2.00
Closing balance (C) = (A) + (B)	12.00
Depreciation:	
Opening balance (D)	2.50
Depreciation during the year (E) (0.5 + 0.05)	0.55
Closing balance (F) = (D) + (E)	3.05
Net balance (C) - (F)	8.95

The changes in the carrying value of investment properties for the year ended 31st March, 20X2 are as follows:

Amount recognized in Profit and Loss with respect to Investment Properties

Particulars	**Period ending 31st March, 20X2 (₹ in crores)**
Rental income from investment properties (0.75 + 0.25)	1.00
Less: Direct operating expenses generating rental income (5 + 1 + 2.5 + 1.5 + 2 + 1)	(0.13)
Profit from investment properties before depreciation and indirect expenses	0.87
Less: Depreciation	(0.55)
Profit from earnings from investment properties before indirect expenses	0.32

© The Institute of Chartered Accountants of India

Disclosure Note on Investment Properties acquired by the entity

The investment properties consist of Property A and Property B. As at 31st March, 20X2, the fair value of the properties is ₹ 10.50 crores. The valuation is performed by independent valuers, who are specialists in valuing investment properties. A valuation model as recommended by International Valuation Standards Committee has been applied. The Company considers factors like management intention, terms of rental agreements, area leased out, life of the assets etc. to determine classification of assets as investment properties.

The Company has no restrictions on the realisability of its investment properties and no contractual obligations to purchase, construct or develop investment properties or for repairs, maintenance and enhancements.

Description of valuation techniques used and key inputs to valuation on investment properties:

Valuation technique	Significant unobservable inputs	Range (Weighted average)
Discounted cash flow (DCF) method	- Estimated rental value per sq. ft. per month - Rent growth per annum - Discount rate	- ₹ 50 to ₹ 60 - 10% every 3 years - 12% to 13%

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

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

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

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

© The Institute of Chartered Accountants of India

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

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

© The Institute of Chartered Accountants of India

FOR SHORTCUT TO IND AS WISDOM: SCAN ME!

TEST YOUR KNOWLEDGE

Questions

1. On 28th February, 20X1, Entity X becomes committed to a plan to sell a property. However, it plans certain renovations to increase its value prior to selling it. The renovations are expected to be completed within a short span of time i.e., 2 months.

   Comment whether the property can be classified as held for sale at the reporting date i.e. 31st March, 20X1.

2. On 1st March, 20X1, entity R decides to sell one of its factories. An agent is appointed and the factory is actively marketed. As on 31st March, 20X1, it is expected that the factory will be sold by 28th February, 20X2. However, in May 20X1, the market price of the factory deteriorated. Entity R believed that the market would recover and thus did not reduce the price of the factory. The company's accounts are authorised for issue on 26th June, 20X1.

   Recommend whether the factory should be shown as held for sale as on 31st March, 20X1.

3. On 1st June, 20X1, entity X plans to sell a group of assets and liabilities, which is classified as a disposal group. On 31st July, 20X1, the Board of Directors approves and becomes committed to the plan to sell the manufacturing unit by entering into a firm purchase commitment with entity Y. However, since the manufacturing unit is regulated, the approval from the regulator is needed for sale. The approval from the regulator is customary and highly probable to be received by 30th November, 20X1 and the sale is expected to be completed by 31st March, 20X2. Entity X follows December year end.

© The Institute of Chartered Accountants of India

Sensitivity: Public (C4)

The assets and liabilities attributable to this manufacturing unit are as under:

(Amount in ₹)

Particulars	**Carrying value as on 31st December, 20X0**	**Carrying value as on 31st July, 20X1**
Goodwill	500	500
Plant and Machinery	1,000	900
Building	2,000	1,850
Debtors	850	1,050
Inventory	700	400
Creditors	(300)	(250)
Loans	(2,000)	(1,850)
	2,750	2,600

The fair value of the manufacturing unit as on 31st December, 20X0 is ₹ 2,000 and as on 31st July, 20X1 is ₹ 1,850. The cost to sell is ₹ 100 on both these dates. The disposal group is not sold at the period end i.e., 31st December, 20X1. The fair value as on 31st December, 20X1 is lower than the carrying value of the disposal group as on that date.

Required:

1. Assess whether the manufacturing unit can be classified as held for sale and reasons there for. If yes, then at which date?
2. Measure the manufacturing unit on the date of classification as held for sale.
3. Measure the manufacturing unit at the end of the year.

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

Asset/ (liability)	**Carrying amount as on 31st March, 20X1 (In ₹ '000)**
Attributed goodwill	200
Intangible assets	950
Financial asset measured at fair value through other comprehensive income	300

© The Institute of Chartered Accountants of India

Sensitivity: Public (C4)

Property, plant & equipment	1,100
Deferred tax asset	250
Current assets – inventory, receivables and cash balances	600
Current liabilities	(850)
Non-current liabilities – provisions	(300)
Total	**2,250**

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

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

Asset/ (liability)	**Carry amount as on 15th September 20X1 (In ₹ '000)**
Attributed goodwill	200
Intangible assets	930
Financial asset measured at fair value through other comprehensive income	360
Property, plant & equipment	1,020
Deferred tax asset	250
Current assets – inventory, receivables and cash balances	520
Current liabilities	(870)
Non-current liabilities – provisions	(250)
Total	**2,160**

Entity A proposed to sell the disposal group at ₹ 19,00,000. It estimates that the costs to sell will be ₹ 70,000. This cost consists of professional fee to be paid to external lawyers and accountants.

As at 31st March 20X2, there has been no change to the plan to sell the disposal group and entity A still expects to sell it within one year of initial classification. Mr. X, an accountant of

© The Institute of Chartered Accountants of India

Sensitivity: Public (C4)

Entity A remeasured the following assets / liabilities in accordance with respective standards as on 31st March 20X2:

Available for sale:	(In ₹ '000)
Financial assets	410
Deferred tax assets	230
Current assets- Inventory, receivables and cash balances	400
Current liabilities	900
Non- current liabilities- provisions	250

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

Compute the value of all assets/ labilities within the disposal group as on the following dates in accordance with Ind AS 105:

(a) 15 September, 20X1 and

(b) 31st March, 20X2

5. CK Ltd. prepares the financial statement under Ind AS for the quarter and the year ended 30th June, 20X1. During the 3 months ended 30th June, 20X1, the following events occurred:

On 1st April, 20X1, the Company has decided to sell one of its divisions as a going concern following a recent change in its geographical focus. The proposed sale would involve the buyer acquiring the non-monetary assets (including goodwill) of the division, with the Company collecting any outstanding trade receivables relating to the division and settling any current liabilities.

On 1st April, 20X1, the carrying amount of the assets of the division were as follows:

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

From 1st April, 20X1, the Company has started to actively market the division and has received number of serious enquiries. On 1st April, 20X1 the directors estimated that they would receive ₹ 32,00,000 from the sale of the division. Since 1st April, 20X1, market condition has improved and as on 1st August, 20X1 the Company received and accepted a firm offer to purchase the division for ₹ 33,00,000.

© The Institute of Chartered Accountants of India

Sensitivity: Public (C4)

The sale is expected to be completed on 30th September, 20X1 and ₹ 33,00,000 can be assumed to be a reasonable estimate of the value of the division as on 30th June, 20X1. During the period from 1st April to 30th June inventories of the division costing ₹ 8,00,000 were sold for ₹ 12,00,000. At 30th June, 20X1, the total cost of the inventories of the division was ₹ 9,00,000. All of these inventories have an estimated net realisable value that is in excess of their cost.

Suggest how the proposed sale of the division will be reported in the interim financial statements for the quarter ended 30th June, 20X1 giving relevant explanations.

6. Identify which of the following is a disposal group at 31st March 20X1:

   (1) On 21st March 20X1, XYZ announced the Board's intention to sell its shares in a subsidiary company, Alpha, contingent upon the approval of Alpha's shareholders. It seems unlikely that approval will be granted in the near future and no specific potential buyer has been identified.

   (2) PQR has entered into a contract to sell the entire delivery fleet of vehicles operated from its warehouse to a competitor, ABC, on 14th March 20X1. The assets will be transferred on 28th April 20X1 from which date the Group will outsource its delivery activities to another company, LMN.

   (3) On 16th January 20X1, DEF's management and shareholders approved a plan to sell its retail business in Mumbai and a consultant is hired to manage the sale. As at 31st March 20X1 agreement had been signed although due diligence and the negotiation of final terms are still in process. The transaction is expected to be completed in April 20X1.

Answers

1. The property cannot be classified as held for sale at the balance sheet date as it is not available for sale immediately in its present condition. Although the renovations are expected to be completed within a short span 2 months, this fact is not relevant for classification. The delay in the timing of the transfer of the property imposed by the Entity X demonstrates that the property is not available for immediate sale.

However, if the PPE meets the criteria for held for sale by 30th April, 20X1 (i.e., 2 months from 28th February, 20X1) and the accounts are not authorised by that date, then necessary disclosures need to be given in the financial statements.

2. The factory ceases to meet the definition of held for sale post the balance sheet date but before the financial statements are authorised for issue, as it is not actively marketed at a

© The Institute of Chartered Accountants of India

Sensitivity: Public (C4)

reasonable price. But, since the market conditions deteriorated post the balance sheet date, the asset will be classified as held for sale as at 31st March, 20X1.

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

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

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

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

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

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

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

Following steps need to be followed:

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

This has been done and the carrying value of the disposal group as on 31st July, 20X1 is determined at ₹ 2,600. The difference between the carrying value as on 31st December, 20X0 and 31st July, 20X1 is accounted for as per the relevant Ind AS.

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

The fair value less cost to sell of the disposal group as on 31st July, 20X1 is ₹ 1,750 (i.e. 1,850 - 100). This is lower than the carrying value of ₹ 2,600. Thus, an impairment loss needs to be recognised and allocated first towards goodwill and thereafter pro-rata between non-current assets of the disposal group which are within the scope of Ind AS 105 based on their carrying value.

© The Institute of Chartered Accountants of India

Sensitivity: Public (C4)

Thus, the assets will be measured as under:

Particulars	Carrying value – 31st July, 20X1	Impairment	Carrying value as per Ind AS 105 – 31st July, 20X1
Goodwill	500	(500)	-
Plant and Machinery	900	(115)	785
Building	1,850	(235)	1,615
Debtors	1,050	-	1,050
Inventory	400	-	400
Creditors	(250)	-	(250)
Loans	(1,850)	-	(1,850)
	2,600	(850)	1,750

Measurement of the manufacturing unit as on the date of classification as at the year end

The measurement as at the year-end shall be on similar lines as done above.

The assets and liabilities in the disposal group not within the scope of this Standard are measured as per the respective Standards.

The fair value less cost to sell of the disposal group as a whole is calculated. This fair value less cost to sell as at the year-end shall be compared with the carrying value as at the date of classification as held for sale. It is provided that the fair value as on the year end is less than the carrying amount as on that date – thus the impairment loss shall be allocated in the same way between the assets of the disposal group falling within the scope of this standard as shown above.

4. (a) As at 15th September, 20X1

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

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

© The Institute of Chartered Accountants of India

Sensitivity: Public (C4)

Asset/ (liability)	Carrying value as at 15th September, 20X1	Impairment	Revised carrying value as per Ind AS 105
Attributed goodwill	200	(200)	-
Intangible assets	930	(62)	868
Financial asset measured at fair value through other comprehensive income	360	-	360
Property, plant & equipment	1,020	(68)	952
Deferred tax asset	250	-	250
Current assets – inventory, receivables and cash balances	520	-	520
Current liabilities	(870)	-	(870)
Non-current liabilities – provisions	(250)	-	(250)
Total	2,160	(330)	1,830

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

(b) As on 31 March, 20X2:

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

© The Institute of Chartered Accountants of India

Sensitivity: Public (C4)

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

5. The decision to offer the division for sale on 1st April, 20X1 means that from that date the division has been classified as held for sale. The division available for immediate sale, is being actively marketed at a reasonable price and the sale is expected to be completed within one year.

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

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

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

© The Institute of Chartered Accountants of India

Sensitivity: Public (C4)

The Property, Plant and Equipment shall not be depreciated after 1st April, 20X1 so its carrying value at 30th June, 20X1 will be ₹ 20,00,000 only. The inventories of the division will be shown at ₹ 9,00,000.

The division will be regarded as discontinued operation for the quarter ended 30th June, 20X1. It represents a separate line of business and is held for sale at the year end.

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

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

6. **Presented as held for sale**

(2) PQR's fleet is classified as held for sale because it constitutes a group of assets to be sold in their present condition and the sale is highly probable at the reporting date (as a contract has been entered into).

(3) DEF's sale of its retail business will not be completed until the final terms (e.g. of purchase price) are agreed. However, the business is ready for immediate sale and the sale is highly probable unless other evidence after the reporting date but before the financial statements are approved for issue, comes to light to indicate the contrary.

Not presented as held for sale

(1) XYZ's shares in Alpha are not available for an immediate sale as shareholders' approval is required. Also no specific potential buyer has been identified. In taking these facts into consideration for the assessment of whether the sale is highly probable, it is clearly not highly probable.

© The Institute of Chartered Accountants of India

Sensitivity: Public (C4)

FOR SHORTCUT TO IND AS WISDOM: SCAN ME!

TEST YOUR KNOWLEDGE

QUESTIONS

1. A lessee enters into a ten-year contract with a lessor (freight carrier) to transport a specified quantity of goods. Lessor uses rail wagons of a particular specification and has a large pool of similar rail wagons that can be used to fulfil the requirements of the contract. The rail wagons and engines are stored at lessor's premises when they are not being used to transport goods. Costs associated with substituting the rail wagons are minimal for lessor.

   Whether the lessor has substantive substitutions rights and whether the arrangement contains a lease?

2. Customer M enters into a 20-year contract with Energy Supplier S to install, operate and maintain a solar plant for M's energy supply. M designed the solar plant before it was constructed – M hired experts in solar energy to assist in determining the location of the plant and the engineering of the equipment to be used. M has the exclusive right to receive and the obligation to take any energy produced. Whether it can be established that M is having the right to control the use of identified asset?

3. A Customer enters into a ten-year contract with a Company (a ship owner) for the use of an identified ship. The customer decides whether and what cargo will be transported, and when and to which ports the ship will sail throughout the period of use, subject to restrictions specified in the contract. These restrictions prevent the company from sailing the ship into waters at a high risk of piracy or carrying explosive materials. The company operates and maintains the ship and is responsible for safe passage.

   Does the customer have the right to direct how and for what purpose the ship is to be used throughout the period of use and whether the arrangement contains a lease?

© The Institute of Chartered Accountants of India

Sensitivity: Public (C4)

4. A Lessee enters into a ten-year lease contract with a Lessor to use equipment. The contract includes maintenance services (as provided by the lessor). The Lessor obtains its own insurance for the equipment. Annual payments are ₹ 10,000 (₹ 1,000 related to maintenance services and ₹ 500 to insurance costs).

   The Lessee is able to determine that similar maintenance services and insurance costs are offered by third parties for ₹ 2,000 and ₹ 500 a year, respectively. The Lessee is unable to find an observable stand-alone rental amount for similar equipment because none is leased without related maintenance services provided by the lessor.

   How would the Lessee allocate the consideration to the lease component?

5. A Lessee enters into a non-cancellable lease contract with a Lessor to lease a building. Initially, the lease is for five years, and the lessee has the option to extend the lease by another five years at the same rental.

   To determine the lease term, the lessee considers the following factors:

   - Market rentals for a comparable building in the same area are expected to increase by 10% over the ten-year period covered by the lease. At inception of the lease, lease rentals are in accordance with current market rents.
   - The lessee intends to stay in business in the same area for at least 20 years.
   - The location of the building is ideal for relationships with suppliers and customers.

   What should be the lease term for lease accounting under Ind AS 116?

6. A Lessee enters into a lease of a five-year-old machine. The non-cancellable lease term is 15 years. The lessee has the option to extend the lease after the initial 15-year period for optional periods of 12 months each at market rents.

   To determine the lease term, the lessee considers the following factors:

   - The machine is to be used in manufacturing parts for a type of plane that the lessee expects will remain popular with customers until development and testing of an improved model are completed in approximately 15 years.
   - The cost to install the machine in lessee's manufacturing facility is significant.
   - The non-cancellable term of lessee's manufacturing facility lease ends in 15 years, and the lessee has an option to renew that lease for another twelve years.
   - Lessee does not expect to be able to use the machine in its manufacturing process for other types of planes without significant modifications.
   - The total remaining life of the machine is 30 years.

   What should be the lease term for lease accounting under Ind AS 116?

© The Institute of Chartered Accountants of India

Sensitivity: Public (C4)

7. A Company leases a manufacturing facility. The lease payments depend on the number of operating hours of the manufacturing facility, i.e., the lessee has to pay ₹ 2,000 per hour of use. The annual minimum payment is ₹ 2,00,00,000. The expected usage per year is 20,000 hours.

   Whether the said payments be included in the calculation of lease liability under Ind AS 116?

8. Entity X (lessee) entered into a lease agreement ('lease agreement') with Entity Y (lessor) to lease an entire floor of a shopping mall for a period of 9 years. The annual lease rent of ₹ 70,000 is payable at year end. To carry out its operations smoothly, Entity X simultaneously entered into another agreement ('facilities agreement') with Entity Y for using certain other facilities owned by Entity Y such as passenger lifts, DG sets, power supply infrastructure, parking space etc., which are specifically mentioned in the agreement, for annual service charges amounting to ₹ 1,00,000. As per the agreement, the ownership of the facilities shall remain with Entity Y. Lessee's incremental borrowing rate is 10%.

   The facilities agreement clearly specifies that it shall be co-existent and coterminous with 'lease agreement'. The facility agreement shall stand terminated automatically on termination or expiry of 'lease agreement'.

   Entity X has assessed that the stand-alone price of 'lease agreement' is ₹ 1,20,000 per year and stand-alone price of the 'facilities agreement' is ₹ 80,000 per year. Entity X has not elected to apply the practical expedient in paragraph 15 of Ind AS 116 of not to separate non-lease component(s) from lease component(s) and accordingly it separates non-lease components from lease components.

   How will Entity X account for lease liability as at the commencement date?

9. Entity X is an Indian entity whose functional currency is Indian Rupee. It has taken a plant on lease from Entity Y for 5 years to use in its manufacturing process for which it has to pay annual rentals in arrears of USD 10,000 every year. On the commencement date, exchange rate was USD = ₹ 68. The average rate for Year 1 was ₹ 69 and at the end of year 1, the exchange rate was ₹ 70. The incremental borrowing rate of Entity X on commencement of the lease for a USD borrowing was 5% p.a.

   How will entity X measure the right of use (ROU) asset and lease liability initially and at the end of Year 1?

ANSWERS

1. In this case, the rail wagons are stored at lessor's premises, and it has a large pool of similar rail wagons and substitution costs to be incurred are minimal. Thus, the lessor has the practical ability to substitute the asset. If at any point, the same becomes economically

© The Institute of Chartered Accountants of India

Sensitivity: Public (C4)

beneficial for the lessor to substitute the wagons, he can do so and hence, the lessor's substitution rights are substantive, and the arrangement does not contain a lease.

2. In this case, the nature of the solar plant is such that all the decisions about how and for what purpose the asset is used are predetermined because:

– the type of output (i.e. energy) and the production location are predetermined in the agreement; and

– when, whether and how much energy is produced is influenced by the sunlight and the design of the solar plant.

Because M designed the solar plant and thereby predetermined any decisions about how and for what purpose it is used, M is considered to have the right to direct the use. Although regular maintenance of the solar plant may increase the efficiency of the solar panels, it does not give the supplier the right to direct how, and for what purpose the solar plant is used. Hence, M has a right to control the use of asset.

3. The customer has the right to direct the use of the ship because the contractual restrictions are merely protective rights that protect the company's investment in the ship and its personnel. In the scope of its right of use, the customer determines how and for what purpose the ship is used throughout the ten-year period because it decides whether, where and when the ship sails, as well as the cargo that it will transport.

The customer has the right to change these decisions throughout the period of use and hence, the contract contains a lease.

4. The observable stand-alone price for maintenance services is ₹ 2,000. There is no observable stand-alone price for the lease. Further, the insurance cost does not transfer a good or service to the lessee and therefore, it is not a separate lease component.

Thus, the Lessee allocates ₹ 8,000 (₹ 10,000 – ₹ 2,000) to the lease component.

5. After considering all the stated factors, the lessee concludes that it has a significant economic incentive to extend the lease.

Thus, for the purpose of lease accounting under Ind AS 116, the lessee uses a lease term of ten years.

6. The lessee notes that the terms for the optional renewal provide no economic incentive and the cost to install is significant. The lessee has no incentive to make significant modifications to the machine after the initial 15-year period. Therefore, the lessee does not expect to have a business purpose for using the machine after the non-cancellable lease term of 15 years.

Thus, the lessee concludes that the lease term consists of 15-year non-cancellable period only.

© The Institute of Chartered Accountants of India

Sensitivity: Public (C4)

7. The said lease contains in-substance fixed payments of ₹ 2,00,00,000 per year, which are included in the initial measurement of the lease liability under Ind AS 116.

   However, the additional ₹ 2,00,00,000 that the company expects to pay per year are variable payments that do not depend on an index or rate and, thus, are not included in the initial measurement of the lease liability but, are expensed when the over-use occurs.

8. Entity X identifies that the contract contains lease of premises and non-lease component of facilities availed. As Entity X has not elected to apply the practical expedient as provided in paragraph 15, it will separate the lease and non-lease components and allocate the total consideration of ₹ 1,70,000 to the lease and non-lease components in the ratio of their relative stand-alone selling prices as follows:

Particulars	Stand-alone Prices	% of total Stand-alone Price	Allocation of consideration
	₹		₹
Building rent	1,20,000	60%	1,02,000
Service charge	80,000	40%	68,000
Total	**2,00,000**	**100%**	**1,70,000**

As Entity X's incremental borrowing rate is 10%, it discounts lease payments using this rate and the lease liability at the commencement date is calculated as follows:

Year	Lease Payment (A)	Present value factor @ 10% (B)	Present value of lease payments (A x B = C)
Year 1	1,02,000	0.909	92,718
Year 2	1,02,000	0.826	84,252
Year 3	1,02,000	0.751	76,602
Year 4	1,02,000	0.683	69,666
Year 5	1,02,000	0.621	63,342
Year 6	1,02,000	0.564	57,528
Year 7	1,02,000	0.513	52,326
Year 8	1,02,000	0.467	47,634
Year 9	1,02,000	0.424	43,248
Lease Liability at commencement date			**5,87,316**

Further, ₹ 68,000 allocated to the non-lease component of facility used will be recognised in profit or loss as and when incurred.

© The Institute of Chartered Accountants of India

Sensitivity: Public (C4)

9. On initial measurement, Entity X will measure the lease liability and ROU asset as under:

Year	Lease Payments (USD)	Present Value factor @ 5%	Present Value of Lease Payment	Conversion rate (spot rate)	INR value
1	10,000	0.952	9,520	68	6,47,360
2	10,000	0.907	9,070	68	6,16,760
3	10,000	0.864	8,640	68	5,87,520
4	10,000	0.823	8,230	68	5,59,640
5	10,000	0.784	7,840	68	5,33,120
Total			**43,300**		**29,44,400**

As per Ind AS 21 *The Effects of Changes in Foreign Exchange Rates*, monetary assets and liabilities are restated at each reporting date at the closing rate and the difference due to foreign exchange movement is recognised in profit and loss whereas non-monetary assets and liabilities carried measured in terms of historical cost in foreign currency are not restated.

Accordingly, the ROU asset in the given case being a non-monetary asset measured in terms of historical cost in foreign currency will not be restated but the lease liability being a monetary liability will be restated at each reporting date with the resultant difference being taken to profit and loss.

At the end of Year 1, the lease liability will be measured in terms of USD as under:

Lease Liability:

Year	Initial Value (USD) (a)	Lease Payment (b)	Interest @ 5% (c) = (a x 5%)	Closing Value (USD) (d = a + c - b)
1	43,300	10,000	2,165	35,465

Interest at the rate of 5% will be accounted for in profit and loss at average rate of ₹ 69 (i.e., USD 2,165 x 69) = ₹ 1,49,385.

Particulars		Dr. (₹)	Cr. (₹)
Interest Expense	Dr.	1,49,385	
To Lease liability			1,49,385

Lease payment would be accounted for at the reporting date exchange rate, i.e. ₹ 70 at the end of year 1

© The Institute of Chartered Accountants of India

Sensitivity: Public (C4)

Particulars		Dr. (₹)	Cr. (₹)
Lease liability	Dr.	7,00,000	
To Cash			7,00,000

As per the guidance above under Ind AS 21, the lease liability will be restated using the reporting date exchange rate i.e., ₹ 70 at the end of Year 1. Accordingly, the lease liability will be measured at ₹ 24,82,550 (35,465 x ₹ 70) with the corresponding impact due to exchange rate movement of ₹ 88,765 (24,82,550 – (29,44,400 + 1,49,385 – 700,000) taken to profit and loss.

At the end of year 1, the ROU asset will be measured as under:

Year	Opening Balance (₹)	Depreciation (₹)	Closing Balance (₹)
1	29,44,400	5,88,880	23,55,520

© The Institute of Chartered Accountants of India

Sensitivity: Public (C4)

FOR SHORTCUT TO IND AS WISDOM: SCAN ME!

TEST YOUR KNOWLEDGE

Questions

1. Entity A purchased cattle at an auction on 30th June 20X1

Purchase price at 30th June 20X1	₹ 1,00,000
Costs of transporting the cattle back to the entity's farm	₹ 1,000
Sales price of the cattle at 31st March, 20X2	₹ 1,10,000

The company would have to incur similar transportation costs if it were to sell the cattle at auction, in addition to an auctioneer's fee of 2% of sales price. The auctioneer charges 2% of the selling price, from both, the buyer as well as the seller.

Calculate the amount at which cattle is to be recognised in books on initial recognition and at year end 31st March, 20X2. Show corresponding journal entries.

2. XY Ltd. is a farming entity where cows are milked on a daily basis. Milk is kept in cold storage immediately after milking and sold to retail distributors on a weekly basis. On 1st April 20X1, XY Ltd. had a herd of 500 cows which were all three years old.

During the year, some of the cows became sick and on 30th September 20X1, 20 cows died. On 1st October 20X1, XY Ltd. purchased 20 replacement cows from the market for ₹ 21,000 each. These 20 cows were all one-year old when they were purchased.

On 31st March 20X2, XY Ltd. had 1,000 litres of milk in cold storage which had not been sold to retail distributors. The market price of milk at 31st March 20X2 was ₹ 20 per litre. When selling the milk to distributors, XY Ltd. incurs selling costs of ₹ 1 per litre. These amounts did not change during March 20X2 and are not expected to change during April 20X2.

© The Institute of Chartered Accountants of India

Information relating to fair value and costs to sell is given below:

Date	Fair value of a dairy cow (aged)				Costs to sell a cow
	1 year	1.5 years	3 years	4 years	
1st April 20X1	20,000	22,000	27,000	25,000	1,000
1st October 20X1	21,000	23,000	28,000	26,000	1,000
31st March 20X2	21,500	23,500	29,000	26,500	1,100

The fair value of a 3.5 years old cow on 1st October 20X1 is ₹ 27,000.

Pass necessary journal entries of above transactions with respect to cows in the financial statements of XY Ltd. for the year ended 31st March, 20X2? Also show the amount lying in inventory if any.

3. Company X purchased 100 goats at an auction for ₹ 1,00,000 on 30th September 20X1. Subsequent transportation costs were ₹ 1,000 that is similar to the cost X would have to incur to sell the goat at the auction. Additionally, there would be a 2% selling fee on the market price of the goat to be incurred by the seller.

On 31st March 20X2, the market value of the goat in the most relevant market increases to ₹ 1,10,000. Transportation costs of ₹ 1,000 would have to be incurred by the seller to get the goat to the relevant market. An auctioneer's fee of 2% on the market price of the goat would be payable by the seller.

On 1st June 20X2, X sold 18 goats for ₹ 20,000 and incurred transportation charges of ₹ 150. In addition, there was a 2% auctioneer's fee on the market price of the goat paid by the seller.

On 15th September 20X2, the fair value of the remaining goat was ₹ 82,820. 42 goats were slaughtered on that day, with a total slaughter cost of ₹ 4,200. The total market price of the carcasses on that day was ₹ 48,300, and the expected transportation cost to sell the carcasses is ₹ 420. No other costs are expected.

On 30th September 20X2, the market price of the remaining 40 goat was ₹ 44,800. The expected transportation cost is ₹ 400. Also, there would be a 2% auctioneer's fee on the market price of the goat payable by the seller.

Pass Journal entries for the initial and subsequent measurement for all above transactions. Interim reporting periods are of 30th September and 31 March and the company determines the fair values on these dates for reporting.

© The Institute of Chartered Accountants of India

4. On 1st November, 20X1, C Agro Ltd. purchased 100 goats of special breed from a market for ₹ 10,00,000 with a transaction cost of 2%. Goats fair value decreased from ₹ 10,00,000 to ₹ 9,00,000 as on 31st March, 20X2.

   Determine the fair value on the date of purchase and as on financial year ended 31st March, 20X2 under both the cases viz-

   (i) the transaction costs are borne by the seller and

   (ii) the transaction costs are incurred by the seller and purchaser both

   Also pass journal entries under both the situations on both dates.

5. Analyse whether the following activities fall within the scope of Ind AS 41 with proper reasoning:

   - Managing animal-related recreational activities like Zoo
   - Fishing in the ocean
   - Fish farming
   - Development of living organisms such as cells, bacteria and viruses
   - Growing of plants to be used in the production of drugs
   - Purchase of 25 dogs for security purpose of the company's premises.

Answers

1. **Initial recognition of cattle**

	₹
Fair value less costs to sell (₹ 1,00,000 – ₹ 1,000 - ₹ 2,000)	97,000
Cash outflow (₹ 1,00,000 + ₹ 1,000 + ₹ 2,000)	1,03,000
Loss on initial recognition	6,000
Cattle Measurement at year end	
Fair value less costs to sell (₹ 1,10,000 – 1,000 – (2% x 1,10,000))	1,06,800

At 31st March, 20X2, the cattle is measured at ₹ 1,06,800 i.e. fair value less cost to sell (transportation ₹ 1,000 and the estimated auctioneer's fee of ₹ 2,200). The estimated transportation costs of getting the cattle to the auction of ₹ 1,000 are deducted from the sales price in determining fair value.

© The Institute of Chartered Accountants of India

Journal Entries on 30th June, 20X1

(All figures in ₹)

Biological Asset (Cattle A/c)	Dr.	97,000	
Loss on initial recognition	Dr.	6,000	
To Bank (Purchase and cost of transportation on purchase paid by buyer)			1,03,000
(Being biological asset purchased)			

Journal Entries on 31st March, 20X2

(All figures in ₹)

Biological Asset (Cattle A/c)	Dr.	9,800	
To Gain on remeasurement (P/L A/c)			9,800
(Subsequent measurement of cattle at fair value less costs to sell)			

2. Journal Entries on

(All figures in ₹)

30th September 20X1	Loss (on death of 20 cows) (W.N.)	Dr.	5,20,000	
	To Biological asset			5,20,000
	(Loss booked on death of 20 cows)			
1st October 20X1	Biological Asset (purchase of 20 new cows) (W.N.)	Dr.	4,00,000	
	Loss on initial recognition (of 20 new cows)	Dr.	20,000	
	To Bank			4,20,000
	(Initial recognition of 20 new purchased cows at fair value less costs to sell)			
1st October 20X1	Loss on remeasurement of old cows	Dr.	2,88,000	
	To Biological asset [(1,30,00,000 – 5,20,000) – 1,21,92,000]			2,88,000
	(Subsequent measurement of cows at fair value less costs to sell)			

© The Institute of Chartered Accountants of India

	Biological Asset (4,48,000 – 4,00,000)	Dr.	48,000	
	To Gain on remeasurement of new cows			48,000
	(Subsequent measurement of cows at fair value less costs to sell)			

Inventory (Milk) as at 31st March, 20X2 = ₹ 19,000 [1,000 x (20 – 1)].

Working Note:

Calculation of Biological asset at various dates

Date	Number	Age	Fair Value (₹)	Cost to Sell (₹)	Net (₹)	Biological asset (₹)
1st April 20X1	500	3 years	27,000	1,000	26,000	1,30,00,000
30th September 20X1	(20)	3.5 years	27,000	1,000	26,000	(5,20,000)
1st October 20X1	20	1 year	21,000	1,000	20,000	4,00,000
						1,28,80,000
31st March 20X2	480	4 years	26,500	1,100	25,400	1,21,92,000
	20	1.5 years	23,500	1,100	22,400	4,48,000
						1,26,40,000

3. Value of goat at initial recognition (30th September 20X1) **(All figures are in ₹)**

Biological asset (goat)	Dr.	97,000*	
Loss on initial recognition	Dr.	4,000	
To Bank (Purchase and cost of transportation on purchase paid by buyer)			1,01,000
(Initial recognition of goat at fair value less costs to sell)			

*Fair value of goat = 1,00,000 – 1,000 – 2,000 (2% of 1,00,000) = 97,000

Subsequent measurement at 31st March 20X2 **(All figures are in ₹)**

Biological Assets (Goat)	Dr.	9,800	
To Gain on Sale (Profit & Loss)			9,800
(Subsequent measurement of Goat at fair value less costs to sell (1,06,800** – 97,000))			

** Fair value of goat = 1,10,0000 – 1,000 – 2,200 (2% of 1,10,000) = 1,06,800

© The Institute of Chartered Accountants of India

Sale of goat on 1st June 20X2 **(All figures are in ₹)**

Particulars		Dr. (₹)	Cr. (₹)
Biological Assets (Goats)	Dr.	226	
To Gain on Sale (Profit & Loss)			226
(Subsequent re-measurement of 18 goats at fair value less costs to sell just prior to the point at which they are sold [19,450 - {(1,06,800/100) x 18}])			
Cost to Sales (20,000 – 400 {i.e. 2% of 20,000} – 150)	Dr.	19,450	
To Biological Assets (Goats)			19,450
(Recording a cost of sales figure separately with a corresponding reduction in the value of the biological assets)			
Bank	Dr.	19,450	
Selling expenses (150 + 400)	Dr.	550	
To Revenue			20,000
(Recognition of revenue from sale of goat)			

Transfer of Goat to Inventory on 15th September 20X2 **(All figures are in ₹)**

Particulars		Dr. (₹)	Cr. (₹)
Inventory (48,300 - 420)	Dr.	47,880	
Loss on remeasurement	Dr.	1,176	
To Biological Asset (Goats)			44,856#
To Bank (Slaughtering cost)			4,200
(Transfer of goat to inventory)			

#Note: 44,856 is calculated as the proportion of goat sold using the fair value [(1,06,800+ 226 – 19,450) x 42/82]

Subsequent measurement of goat at 30th September 20X2 **(All figures are in ₹)**

Particulars		Dr. (₹)	Cr. (₹)
Biological Asset (Goats)	Dr.	784	
To Gain on remeasurement			784
(Subsequent measurement of goat at fair value less costs to sell [43,504## – {(1,06,800 + 226 – 19,450) – 44,856}]			

##Fair value of goat = 44,800 – 400 – 896 (2% of 44,800) = 43,504.

4. As per para 12 of Ind AS 41, a biological asset shall be measured on initial recognition and at the end of each reporting period at its fair value less costs to sell. Therefore, regardless of who bears the transaction costs, the transaction costs of 2% are the costs to sell the goats on 1st November 20X1, and therefore, the goats should be measured at their fair value less costs to sell on initial recognition date, i.e., ₹ 9,80,000.

© The Institute of Chartered Accountants of India

Journal Entry

As on 1st November 20X1:

(h) Where transaction costs are borne by the seller:

Biological assets (Goats) A/c	Dr.	9,80,000	
Loss on purchase of biological assets (Goats) A/c	Dr.	20,000	
To Bank A/c			10,00,000

(ii) Where transaction costs are borne by the seller and buyer both:

Biological assets (Goats) A/c	Dr.	9,80,000	
Loss on purchase of biological asset (Goats) A/c	Dr.	40,000	
To Bank A/c			10,20,000

As on 31st March 20X2 – under both the scenarios:

Loss on fair valuation of biological assets A/c	Dr.	98,000	
To Biological assets (Goats) A/c			98,000

[9,80,000 - (9,00,000 - 18,000)]

5.

Activity	Whether in the scope of Ind AS 41?	Remarks
Managing animal-related recreational activities like Zoo	No	Since the primary purpose is to show the animals to public for recreational purposes, there is no management of biological transformation but simply control of the number of animals. Hence it will not fall in the purview of considered in the definition of agricultural activity.
Fishing in the ocean	No	Fishing in ocean is harvesting biological assets from unmanaged sources. There is no management of biological transformation since fish grow naturally in the ocean. Hence, it will not

© The Institute of Chartered Accountants of India

		fall in the scope of the definition of agricultural activity.
Fish farming	Yes	Managing the growth of fish and then harvest for sale is agricultural activity within the scope of Ind AS 41 since there is management of biological transformation of biological assets for sale or additional biological assets.
Development of living organisms such as cells, bacteria viruses	Analysis required	The development of living organisms for research purposes does not qualify as agricultural activity, as those organisms are not being developed for sale, or for conversion into agricultural produce or into additional biological assets. Hence, development of such organisms for the said purposes does not fall under the scope of Ind AS 41. However, if the organisms are being developed for sale or use in dairy products, the activity will be considered as agricultural activity under the scope of Ind AS 41.
Growing of plants to be used in the production of drugs	Yes	If an entity grows plants for using it in production of drugs, the activity will be agricultural activity. Hence it will come under the scope of Ind AS 41.
Purchase of 25 dogs for security purposes of the company's premises	No	Ind AS 41 is applied to account for the biological assets when they relate to agricultural activity. Guard dogs for security purposes do not qualify as agricultural activity, since they are not being kept for sale, or for conversion into agricultural produce or into additional biological assets. Hence, they are outside the scope of Ind AS 41.

© The Institute of Chartered Accountants of India

FOR SHORTCUT TO IND AS WISDOM: SCAN ME!

TEST YOUR KNOWLEDGE

Questions

1. ABC Ltd. has received the following grants from the Government of Delhi for its newly started pharmaceutical business:

   - ₹ 20 lakhs received for immediate start-up of business without any further condition.
   - ₹ 50 lakhs received for research and development of drugs required for the treatment of cardiovascular diseases with following conditions:
     - that drugs should be available to the public at 20% cheaper from current market price; and
     - the drugs should be in accordance with quality prescribed by the World Health Organisation [WHO].
   - Two acres of land (fair Value: ₹ 10 Lakhs) received for set up of plant.
   - ₹ 2 lakhs received for purchase of machinery of ₹ 10 lakhs. Useful life of machinery is 5 years. Depreciation on this machinery is to be charged on straight-line basis.

   Recommend how should ABC Ltd. recognise the government grants in its books of accounts.

2. A Limited received from the government a loan of ₹1,00,00,000 @ 5% payable after 5 years in a bulleted payment. The prevailing market rate of interest is 12%. Interest is payable regularly at the end of each year.

   Calculate the amount of government grant and pass necessary journal entry. Also examine how the government grant be recognised. Also state how the grant will be recognized in the statement of profit or loss assuming that the loan is to finance a depreciable asset.

3. MNC Ltd. has received grant in the nature of exemption of custom duty on capital goods with certain conditions related to export of goods under Export Promotion Capital Goods (EPCG) scheme of Government of India.

© The Institute of Chartered Accountants of India

State whether the same is a government grant under Ind AS 20, Government Grants and Disclosure of Government Assistance? If yes, then how the same is to be accounted for if it is

(a) A grant related to asset; or

(b) A grant related to income.

4. ABC Ltd is a government company and is a first-time adopter of Ind AS. As per the previous GAAP, the contributions received by ABC Ltd. from the government (which holds 100% shareholding in ABC Ltd.) which is in the nature of promoters' contribution have been recognised in capital reserve and treated as part of shareholders' funds in accordance with the provisions of AS 12, Accounting for Government Grants.

   State whether the accounting treatment of the grants in the nature of promoters' contribution as per AS 12 is also permitted under Ind AS 20 Accounting for Government Grants and Disclosure of Government Assistance.

5. Rainbow Limited carries out various projects for which it has either received government financial assistance or is in the process of receiving the same. The company has received two grants of ₹ 1,00,000 each, relating to the following ongoing research and development projects:

   (i) The first grant relates to the "Clean river project" which involves research into the effect of various chemicals waste from the industrial area in Madhya Pradesh. However, no major steps have been completed by Rainbow limited to commence this research as at 31st March, 20X2.

   (ii) The second grant relates to the commercial development of a new equipment that can be used to manufacture eco-friendly substitutes for existing plastic products. Rainbow Limited is confident about the technical feasibility and financial viability of this new technology which will be available for sale in the market by April 20X3.

   In September 20X1, due to the floods near one of its factories, the entire production was lost and Rainbow Limited had to shut down the factory for a period of 3 months. The State Government announced a compensation package for all the manufacturing entities affected due to the floods. As per the scheme, Rainbow Limited is entitled to a compensation based on the average of previous three months' sales figure prior to the floods, for which the company is required to submit an application form on or before 30th June, 20X2 with necessary figures. The financial statements of Rainbow Limited for the year ended 31st March 20X2 are to be adopted on 31st May, 20X2, by which date the claim form would not have been filed with the State Government.

   Suggest the accounting treatment of, if any, for the two grants received and the flood-related compensation in the books of accounts of Rainbow Limited as at 31st March, 20X2.

© The Institute of Chartered Accountants of India

6. An entity opens a new factory and receives a government grant of ₹ 15,000 in respect of capital equipment costing ₹ 1,00,000. It depreciates all plant and machinery at 20% per annum on straight-line basis.

   Show the statement of profit and loss and balance sheet extracts in respect of the grant for first year under both the methods as per Ind AS 20.

7. A company receives a cash grant of ₹ 30,000 on 31st March 20X1. The grant is towards the cost of training young apprentices. Training programme is expected to last for 18 months starting from 1st April 20X1. Actual costs of the training incurred in 20X1-20X2 was ₹ 50,000 and in 20X2-20X3 ₹ 25,000.

   State, how this grant should be accounted for.

8. Entity A is awarded a government grant of ₹ 60,000 receivable over three years (₹ 40,000 in year 1 and ₹ 10,000 in each of years 2 and 3), contingent on creating 10 new jobs and maintaining them for three years. The employees are recruited at a total cost of ₹ 30,000, and the wage bill for the first year is ₹ 1,00,000, rising by ₹ 10,000 in each of the subsequent years.

   Calculate the grant income and deferred income to be accounted for in the books for the years 1, 2 and 3 under the following two situations:

   (a) There is reasonable assurance that the entity will comply with the conditions attaching to them and the grant will be received

   (b) There is no reasonable assurance that the grant will be received.

Answers

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

- ₹ 20 lakhs have been received for immediate start-up of business. This should be recognised in Statement of Profit and Loss immediately as there are no further conditions attached to the grant.
- ₹ 50 lakhs should be recognised in profit or loss on a systematic basis over the periods which the entity recognises as expense the related costs for which the grants are intended to compensate provided that there is reasonable assurance that ABC Ltd. will comply with the conditions attached to the grant.
- Land should be recognised at fair value of ₹ 10 lakhs and government grant should be presented in the balance sheet by setting up the grant as deferred income. Alternatively, deduct the amount of grant from the cost of the asset. In the given case, the land is granted at no cost. It will be presented in the books at nominal value.

© The Institute of Chartered Accountants of India

- ₹ 2 lakhs should be recognised as deferred income and will be transferred to profit and loss over the useful life of the asset. In this case, ₹ 40,000 [₹ 2 lakhs/5] should be credited to profit and loss each year over a period of 5 years. Alternatively, ₹ 2,00,000 will be deducted from the cost of the asset and depreciation will be charged at reduced amount of ₹ 8,00,000 (₹ 10,00,000 – ₹ 2,00,000) every year.

2. The fair value of the loan is calculated at ₹ 74,76,656 (refer Working Note).

Year	Opening Balance	Interest calculated @ 12%	Interest paid @ 5% on ₹ 1,00,00,000 + principal paid	Closing Balance
(a)	(b)	(c) = (b) x 12%	(d)	(e) =(b) + (c) – (d)
1	74,76,656	8,97,200	5,00,000	78,73,856
2	78,73,856	9,44,862	5,00,000	83,18,718
3	83,18,718	9,98,246	5,00,000	88,16,964
4	88,16,964	10,58,036	5,00,000	93,75,000
5	93,75,000	11,25,000	1,05,00,000	Nil

A Limited will recognise ₹ 25,23,344 (₹ 1,00,00,000 – ₹ 74,76,656) as the government grant and will make the following entry on receipt of loan:

Bank Account	Dr.	1,00,00,000	
To Deferred Income			25,23,344
To Loan Account			74,76,656

₹ 25,23,344 is to be recognised in profit or loss on a systematic basis over the periods in which A Limited recognised as expenses the related costs for which the grant is intended to compensate.

If the loan is to finance a depreciable asset. ₹ 25,23,344 will be recognised in profit or loss on the same basis as depreciation.

Working Note:

Particulars	Rs.	Discounting factor@ 12%	Present value taking 12% as the discount rate (Rs.)
Interest @ 5% for Year 1 on loan amount of ₹ 1 crore	5,00,000	0.893	4,46,429
Interest @ 5% for Year 2 on loan amount of ₹ 1 crore	5,00,000	0.798	3,98,597

© The Institute of Chartered Accountants of India

Interest @ 5% for Year 3 on loan amount of ₹ 1 crore	5,00,000	0.712	3,55,890
Interest @ 5% for Year 4 on loan amount of ₹ 1 crore	5,00,000	0.636	3,17,759
Interest @ 5% for Year 5 on loan amount of ₹ 1 crore	5,00,000	0.567	2,83,713
Loan	1,00,00,000	0.567	56,74,269
Present value of loan at the beginning of Year 1			**74,76,656**

The above present value above has been computed on full scale basis.

3. Paragraph 3 of Ind AS 20 states that Government grants are assistance by government in the form of transfers of resources to an entity in return for past or future compliance with certain conditions relating to the operating activities of the entity. They exclude those forms of government assistance which cannot reasonably have a value placed upon them and transactions with government which cannot be distinguished from the normal trading transactions of the entity.

In accordance with the above, in the given case exemption of custom duty under EPCG scheme is a government grant and should be accounted for as per the provisions of Ind AS 20.

Ind AS 20 defines grant related to assets and grants related to income as follows:

"Grants related to asset are government grants whose primary condition is that an entity qualifying for them should purchase, construct or otherwise acquire long-term assets. Subsidiary conditions may also be attached restricting the type or location of the assets or the periods during which they are to be acquired or held. Grants related to income are government grants other than those related to assets."

Presentation

It is pertinent to note that the classification of the grant as related to asset or income will require exercise of judgement and careful examination of the facts, objective and conditions attached to the scheme of the government. Care is also required to ascertain the purpose of the grant and the costs for which the grant is intended to compensate. Based on the evaluation of facts, if it is ascertained that the grant is an asset related grant then the same shall be presented as per paragraphs 24 and 26 of Ind AS 20 which has been stated below:

Presentation of grants related to assets

As per para 24, government grants related to assets, including non-monetary grants at fair value, shall be presented in the balance sheet by setting up the grant as deferred income.

As per para 26, the grant set up as deferred income is recognised in profit or loss on a systematic basis over the useful life of the asset.

© The Institute of Chartered Accountants of India

If it is determined that the grant is related to income then the same shall be presented as follows:

Presentation of grants related to income

As per para 29, grants related to income are presented as part of profit or loss, either separately or under a general heading such as 'Other income'; alternatively, they are deducted in reporting the related expense.

It may be further noted that as per paragraph 12 of Ind AS 20, government grants shall be accounted as follows:

As per para 12, government grants shall be recognised in profit or loss on a systematic basis over the periods in which the entity recognises as expenses the related costs for which the grants are intended to compensate.

In the given case, if based on the terms and conditions of the scheme, the grant received is to compensate the import cost of assets subject to an export obligation as prescribed in the EPCG Scheme; recognition of grant in the statement of profit and loss should be linked to fulfilment of associated export obligations.

However, if the grant received is to compensate the import cost of the asset and based on the examination of the terms and conditions of the grant, if it can be reasonably concluded that conditions relating to export of goods are subsidiary conditions, then it is appropriate to recognise such grant in profit or loss over the life of the underlying asset.

4. Paragraph 2 of Ind AS 20, "Accounting for Government Grants and Disclosure of Government Assistance" inter alia states that the Standard does not deal with government participation in the ownership of the entity.

Since ABC Ltd. is a government company, it implies that government has 100% shareholding in the entity. Accordingly, as per Ind AS 20, the entity needs to determine whether the payment is provided as a shareholder contribution or as a government. Equity contributions will be recorded in equity while grants will be shown in the Statement of Profit and Loss.

Where it is concluded that the contributions are in the nature of government grant, the entity shall apply the principles of Ind AS 20 retrospectively as specified in Ind AS 101 'First Time Adoption of Ind AS'. Ind AS 20 requires all grants to be recognised as income on a systematic basis over the periods in which the entity recognises as expenses the related costs for which the grants are intended to compensate. Unlike AS 12, Ind AS 20 requires the grant to be classified as either a capital or an income grant and does not permit recognition of government grants in the nature of promoter's contribution directly to shareholders' funds.

© The Institute of Chartered Accountants of India

5. **Accounting treatment for:**

   1. **First Grant**

      The first grant for 'Clear River Project' involving research into effects of various chemicals waste from the industrial area in Madhya Pradesh, seems to be unconditional as no details regarding its refund has been mentioned. Even though the research has not been started nor any major steps have been completed by Rainbow Limited to commence the research, yet the grant will be recognised immediately in profit or loss for the year ended 31st March, 20X2.

      Alternatively, in case, the grant is conditional as to expenditure on research, the grant will be recognised in the books of Rainbow Limited over the year the expenditure is being incurred.

   2. **Second Grant**

      The second grant related to commercial development of a new equipment is a grant related to depreciable asset. As per the information given in the question, the equipment will be available for sale in the market from April, 20X3. Hence, by that time, grant relates to the construction of an asset and should be initially recognised as deferred income.

      The deferred income should be recognised as income on a systematic and rational basis over the asset's useful life.

      The entity should recognise a liability in its balance sheets as at 31st March, 20X2 and 31st March, 20X3. Once the equipment starts getting used in the manufacturing process, the deferred grant income of ₹ 100,000 should be recognised over the asset's useful life to compensate for depreciation costs.

      Alternatively, as per Ind AS 20, Rainbow Limited would also be permitted to offset the deferred income of ₹ 100,000 against the cost of the equipment as at 1st April, 20X3.

   3. **For flood related compensation**

      Rainbow Limited will be able to submit an application form only after 31st May, 20X2 ie in the year 20X2-20X3. Although flood happened in September, 20X1 and loss was incurred due to flood in the year 20X1-20X2, the entity should recognise the income from the government grant in the year when the application form related to it is submitted and approved by the government for compensation.

      Since, in the year 20X1-20X2, the application form could not be submitted due to adoption of financials with respect to sales figure before flood occurred, Rainbow Limited should not recognise the grant income as it has not become receivable as at 31st March,20X2.

© The Institute of Chartered Accountants of India

6. (a) **When grant is treated as deferred income**

Statement of profit and loss – An extract

	₹
Depreciation (₹ 1,00,000 x 20%)	(20,000)
Government grant credit (W.N.1)	3,000

Balance Sheet - An extract

		₹
Non-current assets		
Property, plant and equipment	1,00,000	
Less: Accumulated depreciation	(1,00,000 x 20%) (20,000)	80,000
		XXXX
Non-current liabilities		
Government grant	[12,000 – 3,000 (current liability)]	9,000
Current liabilities		
Government grant	(15,000 x 20%)	3,000
		XXXX

Working Note:

1. Government grant deferred income account

	₹		₹
To Profit or loss (15,000 × 20%)	3,000	By Grant cash received	15,000
To Balance c/f	12,000		
	15,000		15,000

(b) When grant is deducted from cost of the asset

Statement of profit and loss – An extract

	₹
Depreciation [(₹ 1,00,000 – 15,000) x 20%]	(17,000)

Balance Sheet – An extract

		₹
Non-current assets		
Property, plant and equipment	(1,00,000-15,000) 85,000	
Less: Accumulated depreciation	(17,000)	68,000

7. As at 31st March 20X1 the grant would be recognised as a liability (deferred income) and presented in the balance sheet as a split between current and non-current amounts.

₹ 20,000 [(12 months / 18 months) x 30,000] is current which would be recognised in the statement of profit and loss for the year ended 31st March, 20X2. The balance amount of ₹ 10,000 will be shown as non-current.

At the end of year 20X1-20X2, there would be a current balance of 10,000 (being the non-current balance at the end of year 20X1-20X1 reclassified as current) in the balance sheet. This would be recognised in profit in the year 20X2-20X3.

Extracts from the financial statements are as follows:

Balance Sheet (extracts)

	31 March 20X1	31 March 20X2	31 March 20X3
Current liabilities			
Deferred income	20,000	10,000	-
Non-current liabilities			
Deferred income	10,000	-	-

Statement of profit and loss (extracts)

	31 March 20X2	31 March 20X3
Method 1		
Other Income - Government grant received	20,000	10,000
Training costs	(50,000)	(25,000)
Method 2		
Training costs (50,000 – 20,000)	30,000	
Training costs (25,000 – 10,000)		15,000

8. (a) When there is reasonable assurance

The grant of ₹ 60,000 should be recognised at the beginning of the first year as receivable and will be compensated for the related costs over three years.

The initial journal entry would be:

Grant Receivable Ac	Dr.	₹ 60,000	
To Deferred Income A/c			₹ 60,000

© The Institute of Chartered Accountants of India

Calculation of grant income and deferred income:

Year	Labour Cost	Grant Income	Computation of Grant Income	Deferred Income at the end of the year	Computation of deferred income at the end of the year
	₹	₹		₹	
1	1,30,000	21,667	60,000 x (130/360)	38,333	(60,000 – 21,667)
2	1,10,000	18,333	60,000 x (110/360)	20,000	(38,333 – 18,333)
3	1,20,000	20,000	60,000 x (120/360)	-	(20,000 – 20,000)
	3,60,000	60,000			

Therefore, grant income to be recognised in the Statement of Profit and Loss for the years 1, 2 and 3 would be ₹ 21,667, ₹ 18,333 and ₹ 20,000 respectively.

The amount of grant that has not yet been credited to the statement of profit and loss i.e. deferred income is to be shown in the balance sheet. Hence deferred income balance as at end of year 1, 2 and 3 are ₹ 38,333, ₹ 20,000 and Nil respectively.

(b) When reasonable assurance is not there

The grant of ₹ 60,000 should be recognised over three years to compensate for the related costs.

The journal entry on receipt of grant at year 1 would be:

Grant Receivable Ac Dr. ₹ 40,000

To Deferred Income A/c ₹ 40,000

Calculation of Grant Income and Deferred Income:

Year	Labour Cost	Grant Income	Computation of Grant Income	Deferred Income at the end of the year	Computation of deferred income at the end of the year
	₹	₹		₹	
1	1,30,000	21,667	60,000 x (130/360)	18,333	(40,000 – 21,667)
2	1,10,000	18,333	60,000 x (110/360)	10,000	(50,000 – 21,667 – 18,333)
3	1,20,000	20,000	60,000 x (120/360)	-	(60,000 – 21,667 – 18,333 – 20,000)
	3,60,000	60,000			

Therefore, Grant income to be recognised in the statement of Profit and Loss for the years 1, 2 and 3 would be ₹ 21,667, ₹ 18,333 and ₹ 20,000 respectively.

Amount of grant that has not yet been credited to the statement of profit and loss i.e; deferred income is to be shown in the balance sheet. Hence, deferred income balance as at the end of year 1, 2 and 3 are ₹ 18,333, ₹ 10,000 and Nil respectively.

© The Institute of Chartered Accountants of India

FOR SHORTCUT TO IND AS WISDOM: SCAN ME!

TEST YOUR KNOWLEDGE

Questions

1. An entity issued 100 shares each to its 1,000 employees subject to service condition of next 2 years. Grant date fair value of the share is ₹ 195 each. There is an expectation 97% of the employees will remain in service at the end of 1st year. However, at the end of 2nd year the expected employees to remain in service would be 91% of the total employees. Calculate the expense for years 1 & 2?

2. An entity issued 50 shares each to its 170 employees subject to service condition of next 2 years. The settlement is to be made in cash. Grant date fair value of the share is ₹ 85 each, however, the fair value as at end of 1st year, 2nd year were ₹ 80 & ₹ 90 respectively. Calculate the expense for years 1 and 2

3. Company P is a holding company for company B. A group share-based payment is being organized in which Parent issues its own equity-shares for the employees of company B. The details are as below –

Number of employees of company B	**100**
Grant date fair value of share	₹ 87
Number of shares to each employee granted	25
Vesting conditions	Immediately

Pass the journal entry in the books of company P & company B?

© The Institute of Chartered Accountants of India

4. An entity P issues share-based payment plan to its employees based on the below details:

Number of employees	100
Fair value at grant date	₹ 25
Market condition	Share price to reach at ₹ 30
Service condition	To remain in service until market condition is fulfilled
Expected completion of market condition	4 years

Define expenses related to such share-based payment plan in each year subject to the below scenarios-

a) Market condition if fulfilled in year 3, or

b) Market condition is fulfilled in year 5.

5. Entity X grants 10 shares each to its 1,000 employees on the conditions as mentioned below-

- To remain in service & entity's profit after tax (PAT) shall reach to ₹ 100 million.
- It is expected that PAT should reach to ₹ 100 million by the end of 3 years.
- Fair value at grant date is ₹ 100.
- Employees expected for vesting right by 1st year 97%, then it revises to 95% by 2nd year and finally to 93% by 3rd year.

Calculate the expenses for next 3 years in respect of share-based payment?

6. At 1st January, 20X0, Ambani Limited grants its CEO an option to take either cash amount equivalent to 800 shares or 990 shares. The minimum service requirement is 2 years. There is a condition to keep the shares for 3 years if shares are opted.

Fair values of the shares	₹
Share alternative fair value (with restrictions)	212
Grant date fair value on 1st January, 20X0	213
Fair value on 31st December, 20X0	220
Fair value on 31st December, 20X1	232

The key management personnel exercises his cash option at the end of 20X2.

Pass the journal entries.

© The Institute of Chartered Accountants of India

7. MINDA issued 11,000 share appreciation rights (SARs) that vest immediately to its employees on 1st April, 20X0. The SARs will be settled in cash. Using an option pricing model, at that date it is estimated that the fair value of a SAR is ₹ 100. SAR can be exercised any time until 31st March, 20X3. It is expected that out of the total employees, 94% at the end of the period on 31st March, 20X1, 91% at the end of next year will exercise the option. Finally, when these were vested i.e. at the end of the 3rd year, only 85% of the total employees exercised the option.

Fair value of SAR	₹
31st March, 20X1	132
31st March, 20X2	139
31st March, 20X3	141

Pass the Journal entries?

8. P Ltd. granted 400 stock appreciation rights (SAR) each to 75 employees on 1st April 20X1 with a fair value ₹ 200. The terms of the award require the employee to provide service for four years in order to earn the award. The fair value of each SAR at each reporting date is as follows:

31st March 20X2	₹ 210
31st March 20X3	₹ 220
31st March 20X4	₹ 215
31st March 20X5	₹ 218

What would be the difference if at the end of the second year of service (i.e. at 31st March 20X3), P Ltd. modifies the terms of the award to require only three years of service?

9. QA Ltd. had on 1st April, 20X1 granted 1,000 share options each to 2,000 employees. The options are due to vest on 31st March, 20X4 provided the employee remains in employment till 31st March, 20X4.

On 1st April, 20X1, the Directors of Company estimated that 1,800 employees would qualify for the option on 31st March, 20X4. This estimate was amended to 1,850 employees on 31st March, 20X2 and further amended to 1,840 employees on 31st March, 20X3.

On 1st April, 20X1, the fair value of an option was ₹ 1.20. The fair value increased to ₹ 1.30 as on 31st March, 20X2 but due to challenging business conditions, the fair value declined thereafter. In September, 20X2, when the fair value of an option was ₹ 0.90, the Directors repriced the option and this caused the fair value to increase to ₹ 1.05. Trading

© The Institute of Chartered Accountants of India

conditions improved in the second half of the year and by 31st March, 20X3 the fair value of an option was ₹ 1.25. QA Ltd. decided that additional cost incurred due to repricing of the options on 30th September, 20X2 should be spread over the remaining vesting period from 30th September, 20X2 to 31st March, 20X4.

Suggest the suitable accounting treatment for these transaction as on 31st March, 20X3.

10. A parent, Company P, grants 30 shares to 100 employees each of its subsidiary, Company S, on condition that the employees remain employed by Company S for three years. Assume that at the outset, and at the end of Years 1 and 2, it is expected that all the employees will remain employed for all the three years. At the end of Year 3, none of the employees has left. The fair value of the shares on grant date is ₹ 5 per share. Company S agrees to reimburse Company P over the term of the arrangement for 75 percent of the final expense recognised by Company S.

What would be the accounting treatment in the books of Company P and Company S?

11. An entity which follows its financial year as per the calendar year grants 1,000 share appreciation rights (SARs) to each of its 40 management employees as on 1st January 20X5. SARs provide the employees with the right to receive (at the date when the rights are exercised) cash equal to the appreciation in the entity's share price since the grant date. All of the rights vest on 31st December 20X6; and they can be exercised during 20X7 and 20X8. Management estimates that, at grant date, the fair value of each SAR is ₹ 11; and it estimates that overall 10% of the employees will leave during the two-year period. The fair values of the SARs at each year end are shown below:

Year	Fair value at year end
31 December 20X5	12
31 December 20X6	8
31 December 20X7	13
31 December 20X8	12

10% of employees left before the end of 20X6. On 31st December 20X7 (when the intrinsic value of each SAR was ₹ 10), six employees exercised their options; and the remaining 30 employees exercised their options at the end of 20X8 (when the intrinsic value of each SAR was equal to the fair value of ₹ 12).

How much expense and liability is to be recognized at the end of each year? Pass the Journal entries.

© The Institute of Chartered Accountants of India

Answers

1.

Year end	% Vest	Expense (current period)
FIRST	97%	100 x 1,000 x 195 x 97% x 1/2 = 94,57,500
SECOND	91%	100 x 1,000 x 195 x 91% x 2/2 – 94,57,500= 82,87,500

2.

Year end	Vest	Expense (current period)
FIRST	1/2	50 x 170 x 80 x 1/2 = 3,40,000
SECOND	2/2	50 x 170 x 90 x 2/2 – 3,40,000 = 4,25,000

- Liability will be re-measured at each reporting date.
- Fair value at the end of the year will be used.

3. **Books of Company P**

Investment in Company B Dr. ₹ 2,17,500

To Equity Capital / Securities Premium (Issue of Shares) ₹ 2,17,500

Books of Company B

Expense Dr. ₹ 2,17,500

To Capital contribution from Parent P ₹ 2,17,500

4. Market conditions are required to be considered while calculating fair value at the grant date. However, service conditions will be considered as per the expected vesting right to be exercised by the employees and would be re-estimated during vesting period. However, if the market-related condition is fulfilled before it is expected then all remaining expenses would immediately be charged off. If market-related condition takes longer than the expected period, then original expected period will be followed.

a) Market condition is fulfilled in year 3:

Year 1	2,500/4 = 625
Year 2	2,500/4 = 625
Year 3	2,500-625-625=1,250
Year 4	NIL

© The Institute of Chartered Accountants of India

b) Market condition is fulfilled in year 5:

Year 1	2,500/4 = 625
Year 2	2,500/4 = 625
Year 3	2,500/4 = 625
Year 4	2,500/4 = 625
Year 5	NIL

5. Entity's PAT is one of the non-market related conditions and hence would be included while making an expectation of vesting shares and there is no requirement to make any changes in the non-market condition whether this is fulfilled or not because it has already been considered in the expectation of vesting rights at the end of each year.

Year -1	1,000 x 10 x 100 x 97% x1/3 = 3,23,333
Year-2	1,000 x 10 x 100 x 95% x 2/3 - 3,23,333 = 3,10,000
Year -3	1,000 x 10 x 100 x 93% x 3/3 - 6,33,333 = 2,96,667

6.

	1st January, 20X0	**31st December, 20X0**	**31st December, 20X1**
Equity alternative (990 x 212)	2,09,880		
Cash alternative (800 x 213)	1,70,400		
Equity option (2,09,880 – 1,70,400)	39,480		
Cash Option (cumulative) (using period end fair value)		88,000	1,85,600
Equity Option (cumulative)		19,740	39,480
Expense for the period			
Equity option		19,740	19,740
Cash Option		88,000	97,600
Total		1,07,740	1,17,340

© The Institute of Chartered Accountants of India

Journal Entries

31st December, 20X0			₹
Employee benefits expenses	Dr.	1,07,740	
To Share-based payment reserve (equity)			19,740
To Share-based payment liability			88,000
(Recognition of Equity option and cash settlement option)			
31st December, 20X1			
Employee benefits expenses	Dr.	1,17,340	
To Share-based payment reserve (equity)			19,740
To Share-based payment liability			97,600
(Recognition of Equity option and cash settlement option)			
Share-based payment liability	Dr.	1,85,600	
To Bank/ Cash			1,85,600
(Settlement in cash)			

7.

Period	Fair value	To be vested	Cumulative	Expense
Start	100	100%	11,00,000	11,00,000
Period 1	132	94%	13,64,880	2,64,880
Period 2	139	91%	13,91,390	26,510
Period 3	141	85%	13,18,350	(73,040)
				13,18,350

Journal Entries

1st April, 20X0			
Employee benefits expenses	Dr.	11,00,000	
To Share-based payment liability			11,00,000
(Fair value of the SAR recognised)			
31st March, 20X1			
Employee benefits expenses	Dr.	2,64,880	

© The Institute of Chartered Accountants of India

To Share-based payment liability (Fair value of the SAR re-measured)		2,64,880
31st March, 20X2		
Employee benefits expenses Dr. To Share-based payment liability (Fair value of the SAR re-measured)	26,510	26,510
31st March, 20X3		
Share-based payment liability Dr. To Employee benefits expenses (Fair value of the SAR reversed)	73,040	73,040
Share-based payment liability Dr. To Cash (Settlement of SAR)	13,18,350	13,18,350

8. **Journal entries in the books of P Ltd (without modification of service period of stock appreciation rights)** **(₹ in lakhs)**

Date	Particulars	Debit	Credit
31.03.20X2	Profit and Loss account Dr. To Liability against SARs (Being expenses liability for stock appreciation rights recognised)	15.75	15.75
31.03.20X3	Profit and Loss account Dr. To Liability for SARs (Being expenses liability for stock appreciation rights recognised)	17.25	17.25
31.03.20X4	Profit and Loss account Dr. To Liability for SARs (Being expenses liability for stock appreciation rights recognised)	15.38	15.38
31.03.20X5	Profit and Loss account Dr. To Liability for SARs (Being expenses liability for stock appreciation rights recognised)	17.02	17.02

© The Institute of Chartered Accountants of India

Journal entries in the books of P Ltd (with modification of service period of stock appreciation rights) **(₹ in lakhs)**

Date	Particulars	Debit	Credit
31.03.20X2	Profit and Loss account Dr. To Liability for SARs (Being expenses liability for stock appreciation rights recognised)	15.75	15.75
31.03.20X3	Profit and Loss account Dr. To Liability for SARs (Being expenses liability for stock appreciation rights recognised)	28.25	28.25
31.03.20X4	Profit and Loss account Dr. To Liability for SARs (Being expenses liability for stock appreciation rights recognised)	20.50	20.50

Working Notes:

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

For the year ended 31st March 20X2

= ₹ 210 x 400 awards x 75 employees x 1 year /4 years of service

= ₹ 15,75,000

For the year ended 31st March 20X3

= ₹ 220 x 400 awards x 75 employees x 2 years /4 years of service - ₹ 15,75,000 previous recognised

= ₹ 33,00,000 - ₹ 15,75,000 = ₹ 17,25,000

For the year ended 31st March 20X4

= ₹ 215 x 400 awards x 75 employees x 3 years/4 years of service - ₹ 33,00,000 previously recognised

= ₹ 48,37,500 - ₹ 33,00,000 = ₹ 15,37,500

© The Institute of Chartered Accountants of India

For the year ended 31st March, 20X5

= ₹ 218 x 400 awards x 75 employees x 4 years / 4 years of service – ₹ 48,37,500 previously recognised

= ₹ 65,40,000 – ₹ 48,37,500 = ₹ 17,02,500

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

For the year ended 31st March 20X2

= ₹ 210 x 400 awards x 75 employees x 1 year / 4 years of service = ₹ 15,75,000

For the year ended 31st March 20X3

= ₹ 220 x 400 awards x 75 employees x 2 years / 3 years of service - ₹ 15,75,000 previous recognised

= ₹ 44,00,000 - ₹ 15,75,000 = ₹ 28,25,000

For the year ended 31st March 20X4

= ₹ 215 x 400 awards x 75 employees x 3 years/ 3 years of service - ₹ 44,00,000 previous recognised

= ₹ 64,50,000 - ₹ 44,00,000 = ₹ 20,50,000.

9. Paragraph 27 of Ind AS 102 requires the entity to recognise the effects of repricing that increase the total fair value of the share-based payment arrangement or are otherwise beneficial to the employee.

If the repricing increases the fair value of the equity instruments granted paragraph B43(a) of Appendix B requires the entity to include the incremental fair value granted (ie the difference between the fair value of the repriced equity instrument and that of the original equity instrument, both estimated as at the date of the modification) in the measurement of the amount recognised for services received as consideration for the equity instruments granted.

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

© The Institute of Chartered Accountants of India

Accordingly, the amounts recognised in years 1 and 2 are as follows:

Year	Calculation	Compensation expense for period	Cumulative compensation expense
		₹	₹
1	[1,850 employees x 1,000 options x ₹ 1.20] x $^1/_3$	7,40,000	7,40,000
2	(1,840 employees x 1,000 options x [(₹ 1.20 x $^2/_3$) + {(₹ 1.05 - 0.90) x 0.5/1.5}] – 7,40,000	8,24,000	15,64,000

Note: Year 3 calculations have not been provided as it was not required in the question.

10. Company S expects to recognise an expense totalling ₹ 15,000 (30 shares x 100 employees x ₹ 5 per share) and, therefore, expects the total reimbursement to be ₹ 11,250 (₹ 15,000 x 75%). Company S therefore reimburses Company P ₹ 3,750 (₹ 11,250 x 1/3) each year.

Accounting by Company S

In each of Years 1 to 3, Company S recognises an expense in profit or loss, the cash paid to Company P, and the balance of the capital contribution it has received from Company P.

Journal Entry			₹
Employee benefits expenses	Dr.	5,000	
To Cash/Bank			3,750
To Equity (Contribution from the parent)			1,250
(To recognise the share-based payment expense and partial reimbursement to parent)			

Accounting by Company P

In each of Years 1 to 3, Company P recognises an increase in equity for the instruments being granted, the cash reimbursed by Company S, and the balance as investment for the capital contribution it has made to Company S.

© The Institute of Chartered Accountants of India

Journal Entry			₹
Investment in Company S	Dr.	1,250	
Cash/Bank	Dr.	3,750	
To Equity			5,000
(To recognise the grant of equity instruments to employees of subsidiary less partial reimbursement from subsidiary)			

11. The amount recognized as an expense in each year and as a liability at each year-end) is as follows:

Year	*Expense* ₹	*Liability* ₹	Calculation of Liability
31 December 20X5	2,16,000	2,16,000	= 36 x 1,000 x 12 x ½
31 December 20X6	72,000	2,88,000	= 36 x 1,000 x 8
31 December 20X7	1,62,000*	3,90,000	= 30 x 1,000 x 13
31 December 20X8	(30,000)**	0	Liability extinguished

* Expense comprises an increase in the liability of ₹ 102,000 and cash paid to those exercising their SARs of ₹ 60,000 (6 x 1,000 x 10).

** Difference of opening liability (₹ 3,90,000) and actual liability paid [₹ 3,60,000 (30 x 1,000 x 12)] is recognised to Profit and loss ie ₹ 30,000.

Journal Entries

31 December 20X5			
Employee benefits expenses	Dr.	2,16,000	
To Share-based payment liability			2,16,000
(Fair value of the SAR recognized)			
31 December 20X6			
Employee benefits expenses	Dr.	72,000	
To Share-based payment liability			72,000
(Fair value of the SAR re-measured)			

© The Institute of Chartered Accountants of India

31 December 20X7			
Employee benefits expenses	Dr.	1,62,000	
To Share-based payment liability			1,62,000
(Fair value of the SAR recognized)			
Share-based payment liability	Dr.	60,000	
To Cash			60,000
(Settlement of SAR)			
31 December 20X8			
Share-based payment liability	Dr.	30,000	
To Employee benefits expenses			30,000
(Fair value of the SAR recognized)			
Share-based payment liability	Dr.	3,60,000	
To Cash			3,60,000
(Settlement of SAR)			

Note: Last two entries can be combined.

© The Institute of Chartered Accountants of India

FOR SHORTCUT TO IND AS WISDOM: SCAN ME!

TEST YOUR KNOWLEDGE

Questions

1. An entity has 100 employees, who are each entitled to five working days of paid sick leaves for each year. Unused sick leave may be carried forward for one calendar year. Sick leave is taken first out of the current year's entitlement and then out of any balance brought forward from the previous year (LIFO basis).

   At 31st March, 20X1, the average unused entitlement is two days per employee. The entity expects, on the basis of experience that is expected to continue, that 92 employees will take no more than five days of paid sick leaves in 20X1-20X2 and that the remaining eight employees will take an average of six and a half days each.

   The entity expects that it will pay an additional twelve days of sick pay as a result of the unused entitlement that has accumulated at 31st March, 20X1 (one and a half days each, for eight employees).

   Comment whether the entity would require to recognize any liability in respect of leaves.

2. A plan provides a monthly pension of 0.3% of final salary for each year of service. The pension is payable from the age of 65.

   Determine the current service cost.

3. A plan pays a benefit of ₹ 140 for each year of service, excluding service before the age of 25. The benefits vest immediately.

   Compute the benefit to be attributed before the age of 25 and after 25?

4. B Pvt. Ltd. has a post-employment medical plan which will reimburse 20% of an employee's post-employment medical costs if the employee leaves after more than ten and less than

© The Institute of Chartered Accountants of India

twenty years of service and 50% of those costs if the employee leaves after twenty or more years of service.

State how would you measure the benefit to be attributed for the employee service for the last 20 years, 10 and 20 years and within 10 years.

5. Cisca Pvt. Ltd. has a headcount of around 1,000 employees in the organisation in 20X0-20X1. As per the company's policy, the employees are given 35 days of privilege leaves (PL), 15 days of sick leaves (SL) and 10 days of casual leaves. Out of the total PL and sick leaves, 10 PL leaves and 5 sick leaves can be carried forward to next year. On the basis of past trends, it has been noted that 200 employees will take 5 days of PL and 2 days of SL and 800 employees will avail 10 days of PL and 5 days of SL.

   Also the company has been incurring profits since 20XX. It has decided in 20X0-20X1 to distribute profits to its employees @ 4% during the year. However, due to the employee turnover in the organisation, the expected pay-out of the Cisca Pvt. Ltd. is expected to be around 3.5%. The profits earned during 20X0-20X1 is ₹ 2,000 crores.

   Cisca Pvt. Ltd. has a post-employment benefit plan also available which is in the nature of defined contribution plan where contribution to the fund amounts to ₹ 100 crores which will fall due within 12 months from the end of accounting period.

   The company has paid ₹ 20 crores to its employees in 20X0-20X1.State what would be the treatment of the short-term compensating absences, profit-sharing plan and the defined contribution plan in the books of Cisca Pvt. Ltd. Also state what would be the treatment, if the contribution paid from defined contribution plan exceeds the contribution due. Further, determine what would be the accounting if the payment from defined contribution plan does not fall due within 12 months from the end of accounting period.

6. OPQ Ltd is a listed company having its corporate office at Nagpur. The company has a branch office at Chennai. The company has been operating in Indian market for the last 10 years.

   The company operates a pension plan that provides a pension of 2.5% of the final salary for each year of service. The benefits become vested after seven years of service.

   On 1st April, 20X8, the company increased the pension to 3% of the final salary for each year of service starting from 1st April, 20X1. On the date of the improvement, the present value of the additional benefits for service from 1st April, 20X1 to 1st April 20X8 was as follows:

   - Employees with more than seven years' service on 1st January 20X8 – ₹ 2,75,000
   - Employees with less than 7 years of service – ₹ 2,21,000 (average 4 years to go).

   Provide the accounting treatment in this case.

© The Institute of Chartered Accountants of India

7. SA Pvt Ltd is engaged in the business of retail having 100 retail outlets across Northern and Southern India. The company's head office is located at Chennai.

   SA Pvt Ltd is a subsidiary of SAG Ltd. SAG Ltd is listed on the National Stock Exchange in India.

   Following information is available for SA Pvt Ltd:

   Plan Assets

   At 1st April, 20X1, the fair value of plan assets was ₹ 10,000.

   Contribution to the plan assets done on 31st March, 20X2 – ₹ 3,000

   Amount paid on 31st March, 20X2 – ₹ 300

   At 31st March, 20X2, the fair value of plan assets was ₹ 14,700

   Actual return on plan assets – ₹ 2,000

   Defined Benefit Obligation

   At 1st April, 20X1, present value of the defined benefit obligation was ₹ 12,000.

   At 31st March, 20X2, present value of the defined benefit obligation was ₹ 15,500.

   Actuarial losses on the obligation for the year ended 31st March, 20X2 were ₹ 100.

   Current Service Cost – ₹ 2,500

   Benefit paid – ₹ 300

   Discount rate used to calculate defined benefit liability - 10%.

   Suggest if there is any amount based on the above-mentioned information that would be taken to other comprehensive income (with workings). Also compute net interest on the net defined benefit liability (asset).

8. A Ltd. prepares its financial statements to 31st March each year. It operates a defined benefit retirement benefits plan on behalf of current and former employees. A Ltd. receives advice from actuaries regarding contribution levels and overall liabilities of the plan to pay benefits. On 1st April, 20X1, the actuaries advised that the present value of the defined benefit obligation was ₹ 6,00,00,000. On the same date, the fair value of the assets of the defined benefit plan was ₹ 5,20,00,000. On 1st April, 20X1, the annual market yield on government bonds was 5%. During the year ended 31st March, 20X2, A Ltd. made contributions of ₹ 70,00,000 into the plan and the plan paid out benefits of ₹ 42,00,000 to retired members. Both these payments were made on 31st March, 20X2.

   The actuaries advised that the current service cost for the year ended 31st March, 20X2 was ₹ 62,00,000. On 28th February, 20X2, the rules of the plan were amended with retrospective effect. These amendments meant that the present value of the defined benefit obligation was increased by ₹ 15,00,000 from that date.

© The Institute of Chartered Accountants of India

During the year ended 31st March, 20X2, A Ltd. was in negotiation with employee representatives regarding planned redundancies. The negotiations were completed shortly before the year end and redundancy packages were agreed. The impact of these redundancies was to reduce the present value of the defined benefit obligation by ₹ 80,00,000. Before 31st March, 20X2, A Ltd. made payments of ₹ 75,00,000 to the employees affected by the redundancies in compensation for the curtailment of their benefits. These payments were made out of the assets of the retirement benefits plan.

On 31st March, 20X2, the actuaries advised that the present value of the defined benefit obligation was ₹ 6,80,00,000. On the same date, the fair value of the assets of the defined benefit plan were ₹ 5,60,00,000.

Examine and present how the above event would be reported in the financial statements of A Ltd. for the year ended 31st March, 20X2 as per Ind AS. Finance cost is to be computed on the opening balances.

9. On 1st April 20X1, the fair value of the assets of XYZ Ltd.'s defined benefit plan were valued at ₹ 20,40,000 and the present value of the defined obligation was ₹ 21,25,000. On 31st March,20X2 the plan received contributions from XYZ Ltd amounting to ₹ 4,25,000 and paid out benefits of ₹ 2,55,000. The current service cost for the financial year ending 31st March 20X2 is ₹ 5,10,000. An interest rate of 5% is to be applied to the plan assets and obligations. The fair value of the plan assets at 31st March 20X2 was ₹ 23,80,000, and the present value of the defined benefit obligation was ₹ 27,20,000.

   Provide a reconciliation from the opening balance to the closing balance for plan assets and defined benefit obligation. Also show how much amount should be recognised in the statement of profit and loss, other comprehensive income and balance sheet?

Answers

1. At 31st March, 20X1, the average unused entitlement is two days per employee. The entity expects, on the basis of experience that is expected to continue, that 92 employees will take no more than five days of paid sick leaves in 20X1-20X2 and that the remaining eight employees will take an average of six and a half days each.

   The entity expects that it will pay an additional twelve days of sick pay as a result of the unused entitlement that has accumulated at 31st March, 20X1 (one and a half days each, for eight employees).

   Therefore, the entity would recognize a liability equal to twelve days of sick pay.

2. Benefit equal to the present value, at the expected retirement date, of a monthly pension of 0.3% of the estimated final salary payable from the expected retirement date until the expected date of death is attributed to each year of service. The current service cost is the present value of that benefit.

© The Institute of Chartered Accountants of India

The present value of the defined benefit obligation is the present value of monthly pension payments of 0.3% of final salary, multiplied by the number of years of service up to the end of the reporting period. The current service cost and the present value of the defined benefit obligation are discounted because pension payments begin at the age of 65.

3. No benefit is attributed to service before the age of 25 because service before that date does not lead to benefits (conditional or unconditional). A benefit of ₹ 140 is attributed to each subsequent year.

4. As per Ind AS 19, the benefit will be attributed till the period the employee service will lead to no material amount of benefits. And service in later years will lead to a materially higher level of benefit than in earlier years. Therefore, for employees expected to leave after twenty or more years, the entity would attribute benefit on a straight-line basis. Service beyond twenty years will lead to no material amount of further benefits. Therefore, the benefit attributed to each of the first twenty years is 2.5% (i.e. 50% divided by 20) of the present value of the expected medical costs.

For employees expected to leave between ten and twenty years, the benefit attributed to each of the first ten years is 2% (20 % divided by 10) of the present value of the expected medical costs. For these employees, no benefit is attributed to service between the end of the tenth year and the estimated date of leaving.

For employees expected to leave within ten years, no benefit is attributed.

5. (i) Cisca Pvt. Ltd. will recognise a liability in its books to the extent of 5 days of PL for 200 employees and 10 days of PL for remaining 800 employees and 2 days of SL for 200 employees and 5 days of SL for remaining 800 employees in its books as an unused entitlement that has accumulated in 20X0-20X1 as short-term compensated absences.

(ii) Cisca Pvt. Ltd. will recognise ₹ 70 crores (2,000 x 3.5%) as a liability and expense in its books of account.

(iii) When an employee has rendered service to an entity during a period, the entity shall recognise the contribution payable to a defined contribution plan in exchange for that service.

Under Ind AS 19, the amount of ₹ 80 crores will be recognised as a liability (accrued expense), after deducting any contribution already paid (100-20) and an expense in the statement of profit and loss. However, if the contribution already paid would have exceeded the contribution due for service before the end of the reporting period, an entity shall recognise that excess as an asset (prepaid expense).

Since the contributions are payable within 12 months from the end of the year in which the employees render the related service, they will not be discounted. However, where contributions to a defined contribution plan do not fall due wholly within twelve months after

© The Institute of Chartered Accountants of India

the end of the period in which the employees render the related service, they shall be discounted using the discount rate.

6. OPQ Ltd increased the pension to 3% of the final salary for each year of service starting from 1st April, 20X1 to 1st April, 20X8.

   The company would recognize the total amount of ₹ 4,96,000 (i.e. ₹ 2,75,000 + ₹ 2,21,000) immediately, as for the purpose of recognition it does not make any difference as to whether the benefits are already vested or not.

7. As per Ind AS 19, net remeasurement of ₹ 900 would be recognized in other comprehensive income.

Computation of Net remeasurement

= Remeasurement – Actuarial loss

= ₹ 1000 (Refer WN - 1) – ₹ 100 (Given in the question) = ₹ 900.

Computation of net interest expense

Particulars	Amount in ₹
Defined benefit liability as at 1st April 20X1 **(A) (Given in the question)**	12,000
Fair value of plan asset as at 1st April 20X1 **(B) (Given in the question)**	(10,000)
Net defined benefit liability **(A - B)**	2,000
Net interest expense (as it is net liability) (Refer note given below)	200

Note:

Net interest expense would be computed on net defined benefit liability using discount rate of 10% given in the question-

= Net defined benefit liability x Discount rate

= 2,000 x 10%

= ₹ 200.

Working Note:

Computation of amount of remeasurement

Particulars	₹
Actual return on plan asset for the year ended 31st March 20X2 **(C) (Given in the question)**	2,000
Less: Interest income on ₹ 10,000 held for 12 months at 10% **(D)**	(1,000)
Remeasurement **(E = C - D)**	1,000

© The Institute of Chartered Accountants of India

8. All figures are ₹ in '000.

On 31st March, 20X2, A Ltd. will report a net pension liability in the statement of financial position. The amount of the liability will be 12,000 (68,000 – 56,000).

For the year ended 31st March, 20X2, A Ltd. will report the current service cost as an operating cost in the statement of profit or loss. The amount reported will be 6,200. The same treatment applies to the past service cost of 1,500.

For the year ended 31st March, 20X2, A Ltd. will report a finance cost in profit or loss based on the net pension liability at the start of the year of 8,000 (60,000 – 52,000). The amount of the finance cost will be 400 (8,000 x 5%).

The redundancy programme represents the partial settlement of the curtailment of a defined benefit obligation. The gain on settlement of 500 (8,000 – 7,500) will be reported in the statement of profit or loss.

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

For the year ended 31st March, 20X2, the remeasurement loss will be 3,400 (Refer W. N.).

Working Note:

Remeasurement of gain or loss

	₹ in '000
Liability at the start of the year (60,000 – 52,000)	8,000
Current service cost	6,200
Past service cost	1,500
Net finance cost	400
Gain on settlement	(500)
Contributions to plan	(7,000)
Remeasurement loss (balancing figure)	3,400
Liability at the end of the year (68,000 – 56,000)	12,000

9. Reconciliation of Plan assets and Defined benefit obligation

	Plan Assets ₹	**Defined benefit obligation ₹**
Fair value/present value as at 1st April 20X1	20,40,000	21,25,000
Interest @ 5%	1,02,000	1,06,250

© The Institute of Chartered Accountants of India

Current service cost		5,10,000
Contributions received	4,25,000	-
Benefits paid	(2,55,000)	(2,55,000)
Return on plan assets (gain) (assets) (balancing figure)	68,000	-
Actuarial Loss (balancing figure)	-	2,33,750
Closing balance as at 31st March, 20X2	23,80,000	27,20,000

In the Statement of Profit and loss, the following will be recognised:	**₹**
Current service cost	5,10,000
Net interest on net defined liability (₹ 1,06,250 – ₹ 1,02,000)	4,250

Defined benefit re-measurements recognised in Other Comprehensive Income:	**₹**
Loss on defined benefit obligation	(2,33,750)
Gain on plan assets	68,000
	(1,65,750)

In the Balance sheet, the following will be recognised:	**₹**
Net defined benefit liability (₹ 27,20,000 – ₹ 23,80,000)	3,40,000

© The Institute of Chartered Accountants of India

FOR SHORTCUT TO IND AS WISDOM: SCAN ME!

TEST YOUR KNOWLEDGE

Questions

1. X Ltd. is operating in the telecom industry. During the Financial Year 20X1-20X2, the Income Tax authorities sent a scrutiny assessment notice under Section 143(2) of the Income-tax Act, 1961, in respect to return filed under Section 139 of this Act for Previous Year 20X0-20X1 (Assessment Year 20X1-20X2) and initiated assessment proceedings on account of a deduction claimed by the company which in the view of the authorities was inadmissible.

   During the financial year 20X1-20X2 itself, the assessment proceedings were completed and the assessing officer did not allow the deduction and raised a demand of ₹ 1,00,00,000 against the company. The company contested such levy and filed an appeal with the Appellate authority. At the end of the financial year 20X1-20X2, the appeal had not been heard. The company is not confident whether that the company would win the appeal. However, the company was advised by its legal counsel that on a similar matter, two appellate authorities of different jurisdictions had given conflicting judgements, one in favour of the assessee and one against the assessee. The legal counsel further stated it had 50% chance of winning the appeal.

   Advise how the company should account for these transactions in the financial year 20X1-20X2.

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

   State the nature of obligation that the entity has in such a case.

© The Institute of Chartered Accountants of India

3. U Ltd. is a large conglomerate with a number of subsidiaries. It is preparing consolidated financial statements as on 31st March 20X2 as per the notified Ind AS. The financial statements are due to be approved for issue on 15th May 20X2. Following are a few transactions that have taken place in some of its subsidiaries during the year:

   G Ltd. is a wholly owned subsidiary of U Ltd. engaged in management consultancy services. On 31st January 20X2, the board of directors of U Ltd. decided to discontinue the business of G Ltd. from 30th April 20X2. They made a public announcement of their decision on 15th February 20X2.

   G Ltd. does not have many assets or liabilities and it is estimated that the outstanding trade receivables and payables would be settled by 31st May 20X2. U Ltd. would collect any amounts still owed by G Ltd.'s customers after 31st May 20X2. They have offered the employees of G Ltd. termination payments or alternative employment opportunities.

   Following are some of the details relating to G Ltd.:

   - On the date of public announcement, it is estimated by G Ltd. that it would have to pay ₹ 540 lakhs as termination payments to employees and the costs for relocation of employees who would remain with the Group would be ₹ 60 lakhs. The actual termination payments totalling to ₹ 520 lakhs were made in full on 15th May 20X2. As per latest estimates made on 15th May 20X2, the total relocation cost is ₹ 63 lakhs.
   - G Ltd. had taken a property on lease, which was expiring on 31st March 20X6. The present value of the future lease rentals (using an appropriate discount rate) is ₹ 430 lakhs. On 15th May 20X2, G Ltd. made a payment to the lessor of ₹ 410 lakhs in return for early termination of the lease.

   The loss after tax of G Ltd. for the year ended 31st March 20X2 was ₹ 400 lakhs. G Ltd. made further operating losses totalling ₹ 60 lakhs till 30th April 20X2.

   Determine the provisions that the Company is required to make as per Ind AS 37?

4. A company manufacturing and supplying process control equipment is entitled to duty draw back if it exceeds its turnover above a specified limit. To claim duty drawback, the company needs to file application within 15 days of meeting the specified turnover. If application is not filed within stipulated time, the Department has discretionary power of giving duty draw back credit. For the year 20X1-20X2 the company has exceeded the specified limit of turnover by the end of the reporting period. However, duty drawback can be claimed on filing of application within the stipulated time or on discretion of the Department if filing of application is late. The application for duty drawback is filed on 20th April, 20X2, which is after the stipulated time of 15 days of meeting the turnover condition. Duty drawback has been credited by the Department on 28th June, 20X2 and financial statements have been approved by the Board of Directors of the company on 26th July, 20X2.

   Identify the treatment of duty drawback credit as per the given information.

© The Institute of Chartered Accountants of India

5. Entity XYZ entered into a contract to supply 1000 television sets for ₹ 2 million. An increase in the cost of inputs has resulted into an increase in the cost of sales to ₹ 2.5 million. The penalty for non- performance of the contract is expected to be ₹ 0.25 million.

   Evaluate whether the contract is onerous and also determine the amount of provision to be made in this regard.

6. Marico has an obligation to restore environmental damage in the area surrounding its factory. Expert advice indicates that the restoration will be carried out in two distinct phases; the first phase requiring expenditure of ₹ 2 million to remove the contaminated soil from the area and the second phase, commencing three years later from the end of first phase, to replant the area with suitable trees and vegetation. The estimated cost of replanting is ₹ 3.5 million. Marico uses a cost of capital (before taxation) of 10% and the expenditure, when incurred, will attract tax relief at the company's marginal tax rate of 30%. Marico has not recognised any provision for such costs in the past and today's date is 31st March 20X2. The first phase of the clean-up will commence in a few months time and will be completed on 31st March 20X3 when the first payment of ₹ 2 million will be made. Phase 2 costs will be paid three years later from the end of first phase.

   Calculate the amount to be provided at 31st March 20X2 for the restoration costs.

Answers

1. Ind AS 37 provides that in rare cases it not clear whether there is a present obligation, for example, in a lawsuit, it may be disputed either whether certain events have occurred or whether those events result in a present obligation. In such a case, an entity should determine whether a present obligation exits at the end of the reporting period by taking account of all available evidence, for example, the opinion of experts.

In the present case, the company is not confident that whether it would win the appeal. By taking into account the opinion of the legal counsel, it is not sure that whether the company would win the appeal. On the basis of such evidence, it is more likely than not that a present obligation exists at the end of the reporting period. Therefore, the entity should recognise a provision. The company should provide for a liability of ₹ 1,00,00,000.

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

(a) an entity has a present obligation (legal or constructive) as a result of a past event;

(b) it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation; and

(c) a reliable estimate can be made of the amount of the obligation. If these conditions are not met, no provision shall be recognised.

© The Institute of Chartered Accountants of India

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

(a) where the settlement of the obligation can be enforced by law; or

(b) in the case of a constructive obligation, where the event (which may be an action of the entity) creates valid expectations in other parties that the entity will discharge the obligation."

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

3. A discontinued operation is one that is discontinued in the period or classified as held for sale at the year end. The operations of G Ltd were discontinued on 30th April 20X2 and therefore, would be treated as discontinued operation for the year ending 31st March 20X3. It does not meet the criteria for held for sale since the company is terminating its business and does not hold these for sale.

As per para 72 of Ind AS 37 'Provisions, Contingent Liabilities and Contingent Assets', restructuring includes sale or termination of a line of business. A constructive obligation to restructure arises when:

(a) an entity has a detailed formal plan for the restructuring

(b) has raised a valid expectation in those affected that it will carry out the restructuring by starting to implement that plan or announcing its main features to those affected by it.

The Board of directors of U Ltd have decided to terminate the operations of G Ltd. from 30th April 20X2. They have made a formal announcement on 15th February 20X2, thus creating a valid expectation that the termination will be implemented. This creates a constructive obligation on the company and requires provisions for restructuring.

A restructuring provision includes only the direct expenditures arising from the restructuring that are necessarily entailed by the restructuring and are not associated with the ongoing activities of the entity.

The termination payments fulfil the above condition. As per Ind AS 10 'Events after Reporting Date', events that provide additional evidence of conditions existing at the

© The Institute of Chartered Accountants of India

reporting date should be reflected in the financial statements. Therefore, the company should make a provision for ₹ 520 lakhs in this respect.

The relocation costs relate to the future conduct of the business and are not liabilities for restructuring at the end of the reporting period. Hence, these would be recognised on the same basis as if they arose independently of a restructuring.

The lease would be regarded as an onerous contract. A provision would be made at the lower of the cost of fulfilling it and any compensation or penalties arising from failure to fulfil it. Hence, a provision shall be made for ₹ 410 lakhs.

Further operating losses relate to future events and do not form a part of the closure provision.

Therefore, the total provision required = ₹ 520 lakhs + ₹ 410 lakhs = ₹ 930 lakhs

4. In the instant case, the condition of exceeding the specified turnover was met at the end of the reporting period and the company was entitled for the duty drawback. However, the application for the same has been filed after the stipulated time. Therefore, credit of duty drawback was discretionary in the hands of the Department. Since the claim was to be accrued only after filing of application, its accrual will be considered in the year 20X2-20X3 only.

Accordingly, the duty drawback credit is a contingent asset as at the end of the reporting period 20X1-20X2, which will be realised when the Department credits the same.

As per para 35 of Ind AS 37, *Provisions, Contingent Liabilities and Contingent Assets*, contingent assets are assessed continually to ensure that developments are appropriately reflected in the financial statements. If it has become virtually certain that an inflow of economic benefits will arise, the asset and the related income are recognised in the financial statements of the period in which the change occurs. If an inflow of economic benefits has become probable, an entity discloses the contingent asset.

In accordance with the above, the duty drawback credit which was contingent asset for the financial year 20X1-20X2 should be recognised as asset and related income should be recognized in the reporting period in which the change occurs. i.e., in the period in which realisation becomes virtually certain, i.e., financial year 20X2-20X3.

5. Ind AS 37 *"Provisions, Contingent Liabilities and Contingent Assets"* defines an onerous contract as a contract in which the unavoidable costs of meeting the obligations under the contract exceed the economic benefits expected to be received under it.

Paragraph 68 of Ind AS 37 states that the unavoidable costs under a contract reflect the least net cost of exiting from the contract, which is the lower of the cost of fulfilling it and

© The Institute of Chartered Accountants of India

any compensation or penalties arising from failure to fulfill it.

In the instant case, cost of fulfilling the contract is ₹ 0.5 million (₹ 2.5 million – ₹ 2 million) and cost of exiting from the contract by paying penalty is ₹ 0.25 million.

In accordance with the above reproduced paragraph, it is an onerous contract as cost of meeting the contract exceeds the economic benefits.

Therefore, the provision should be recognised at the best estimate of the unavoidable cost, which is lower of the cost of fulfilling it and any compensation or penalties arising from failure to fulfill it, i.e., at ₹ 0.25 million (lower of ₹ 0.25 million and ₹ 0.5 million).

6.

Year	Cash Flow	10% Discount factor	Present Value
20X2-20X3	20,00,000	0.909	18,18,000
20X5-20X6	35,00,000	0.683	23,90,500
Provision required at 31st March 20X2			**42,08,500**

The provision is calculated using the pre-tax costs and a pre-tax cost of capital. The fact that the eventual payment will attract tax relief will be reflected in the recognition of a deferred tax asset for the deductible temporary difference (assuming that the recognition criteria for deferred tax assets are met.)

© The Institute of Chartered Accountants of India

FOR SHORTCUT TO IND AS WISDOM: SCAN ME!

TEST YOUR KNOWLEDGE

Questions

1. An asset which cost ₹ 150 has a carrying amount of ₹ 100. Cumulative depreciation for tax purposes is ₹ 90 and the tax rate is 25%. Calculate the tax base and the corresponding deferred tax or liability, if any.

2. On 1st April 20X1, ABC Ltd acquired 100% shares of XYZ Ltd for ₹ 4,373 crore. By 31st March, 20X5, XYZ Ltd had made profits of ₹ 5 crore, which remain undistributed. Based on the tax legislation in India, the tax base investment in XYZ Ltd is its original cost. Show deferred tax treatment.

3. ABC Ltd. acquired 30% of the shares in PQR Ltd. on 1st January, 20X1 for ₹ 1,000 crore. By 31st March, 20X5, PQR Ltd. had made profits of ₹ 50 crore (ABC Ltd.'s share), which remained undistributed. Based on the tax legislation in India, the tax base of the investment in PQR Ltd. is its original cost. Show deferred tax treatment.

4. A company had purchased an asset at ₹ 1,00,000. Estimated useful life of the asset is 5 years and depreciation rate is 20% SLM. Depreciation rate for tax purposes is 25% SLM. The operating profit is ₹ 1,00,000 for all the 5 years. Tax rate is 30% for the next 5 years. Calculate the Book Value as per financial and tax purposes and then DTL.

5. A Ltd. acquired B Ltd. The following assets and liabilities are acquired in a business combination:

₹ 000's

	Fair Value	Carrying amount	Temporary Difference
Plant and Equipment	250	260	(10)
Inventory	120	125	(5)

© The Institute of Chartered Accountants of India

Debtors	200	210	(10)
	570	595	(25)
9% Debentures	(100)	(100)	
	470	495	
Consideration paid	500	500	
Goodwill	30	5	(25)

Assume tax rate as 30%.

Calculate deferred tax asset assuming that the carrying amount is the tax base and prepare the journal entries.

6. B Limited is a newly incorporated entity. Its first financial period ends on 31st March, 20X1. As on the said date, the following temporary differences exist:

   (a) Taxable temporary differences relating to accelerated depreciation of ₹ 9,000. These are expected to reverse equally over next 3 years.

   (b) Deductible temporary differences relating to preliminary expenses of ₹ 4,000 expected to reverse equally over next 4 years.

   It is expected that B Limited will continue to make losses for next 5 years. Tax rate is 30%. Losses can be carried forward but not backwards.

   Discuss the treatment of deferred tax as on 31st March, 20X1.

7. X Ltd. prepares consolidated financial statements to 31st March each year. During the year ended 31st March 20X2, the following events affected the tax position of the group:

   (i) Y Ltd., a wholly owned subsidiary of X Ltd., made a loss adjusted for tax purposes of ₹ 30,00,000. Y Ltd. is unable to utilise this loss against previous tax liabilities. Income-tax Act does not allow Y Ltd. to transfer the tax loss to other group companies. However, it allows Y Ltd. to carry the loss forward and utilise it against company's future taxable profits. The directors of X Ltd. do not consider that Y Ltd. will make taxable profits in the foreseeable future.

   (ii) Just before 31st March, 20X2, X Ltd. committed itself to closing a division after the year end, making a number of employees redundant. Therefore, X Ltd. recognised a provision for closure costs of ₹ 20,00,000 in its statement of financial position as at 31st March, 20X2. Income-tax Act allows tax deductions for closure costs only when the closure actually takes place. In the year ended 31st March 20X3, X Ltd. expects to make taxable profits which are well in excess of ₹ 20,00,000. On 31st March, 20X2, X Ltd. had taxable temporary differences from other sources which were greater than ₹ 20,00,000.

© The Institute of Chartered Accountants of India

(iii) During the year ended 31st March, 20X1, X Ltd. capitalised development costs which satisfied the criteria in paragraph 57 of Ind AS 38 'Intangible Assets'. The total amount capitalised was ₹ 16,00,000. The development project began to generate economic benefits for X Ltd. from 1st January, 20X2. The directors of X Ltd. estimated that the project would generate economic benefits for five years from that date. The development expenditure was fully deductible against taxable profits for the year ended 31st March, 20X2.

(iv) On 1st April, 20X1, X Ltd. borrowed ₹ 1,00,00,000. The cost to X Ltd. of arranging the borrowing was ₹ 2,00,000 and this cost qualified for a tax deduction on 1st April, 20X1. The loan was for a three-year period. No interest was payable on the loan but the amount repayable on 31st March, 20X4 will be ₹ 1,30,43,800. This equates to an effective annual interest rate of 10%. As per the Income-tax Act, a further tax deduction of ₹ 30,43,800 will be claimable when the loan is repaid on 31st March, 20X4.

Explain and show how each of these events would affect the deferred tax assets / liabilities in the consolidated balance sheet of X Ltd. group at 31st March, 20X2 as per Ind AS. Assume the rate of corporate income tax is 20%.

8. PQR Ltd., a manufacturing company, prepares consolidated financial statements to 31st March each year. During the year ended 31st March, 20X2, the following events affected the tax position of the group:

- QPR Ltd., a wholly owned subsidiary of PQR Ltd., incurred a loss adjusted for tax purposes of ₹ 30,00,000. QPR Ltd. is unable to utilise this loss against previous tax liabilities. Income-tax Act does not allow QPR Ltd. to transfer the tax loss to other group companies. However, it allows QPR Ltd. to carry the loss forward and utilise it against company's future taxable profits. The directors of PQR Ltd. do not consider that QPR Ltd. will make taxable profits in the foreseeable future.

- During the year ended 31st March, 20X2, PQR Ltd. capitalised development costs which satisfied the criteria as per Ind AS 38 'Intangible Assets'. The total amount capitalised was ₹ 16,00,000. The development project began to generate economic benefits for PQR Ltd. from 1st January, 20X2. The directors of PQR Ltd. estimated that the project would generate economic benefits for five years from that date. The development expenditure was fully deductible against taxable profits for the year ended 31st March, 20X2.

- On 1st April, 20X1, PQR Ltd. borrowed ₹ 1,00,00,000. The cost to PQR Ltd. of arranging the borrowing was ₹ 2,00,000 and this cost qualified for a tax deduction on 1st April 20X1. The loan was for a three-year period. No interest was payable on the loan but the amount repayable on 31st March 20X4 will be ₹ 1,30,43,800. This equates to an effective annual interest rate of 10%. As per the Income-tax Act, a further tax deduction of ₹ 30,43,800 will be claimable when the loan is repaid on 31st March, 20X4.

© The Institute of Chartered Accountants of India

Explain and show how each of these events would affect the deferred tax assets / liabilities in the consolidated balance sheet of PQR Ltd. group at 31st March, 20X2 as per Ind AS. The rate of corporate income tax is 30%.

9. An entity is finalising its financial statements for the year ended 31st March, 20X2. Before 31st March, 20X2, the government announced that the tax rate was to be amended from 40 per cent to 45 per cent of taxable profit from 30th June, 20X2.

   The legislation to amend the tax rate has not yet been approved by the legislature. However, the government has a significant majority and it is usual, in the tax jurisdiction concerned, to regard an announcement of a change in the tax rate as having the substantive effect of actual enactment (i.e. it is substantively enacted).

   After performing the income tax calculations at the rate of 40 per cent, the entity has the following deferred tax asset and deferred tax liability balances:

Deferred tax asset	₹ 80,000
Deferred tax liability	₹ 60,000

   Of the deferred tax asset balance, ₹ 28,000 related to a temporary difference. This deferred tax asset had previously been recognised in OCI and accumulated in equity as a revaluation surplus.

   The entity reviewed the carrying amount of the asset in accordance with para 56 of Ind AS 12 and determined that it was probable that sufficient taxable profit to allow utilisation of the deferred tax asset would be available in the future.

   Show the revised amount of Deferred tax asset & Deferred tax liability and present the necessary journal entries.

10. On 1st January 20X2, entity H acquired 100% share capital of entity S for ₹ 15,00,000. The book values and the fair values of the identifiable assets and liabilities of entity S at the date of acquisition are set out below, together with their tax bases in entity S's tax jurisdictions. Any goodwill arising on the acquisition is not deductible for tax purposes. The tax rates in entity H's and entity S's jurisdictions are 30% and 40% respectively.

Acquisitions	**Book values ₹'000**	**Tax base ₹'000**	**Fair values ₹'000**
Land and buildings	600	500	700
Property, plant and equipment	250	200	270
Inventory	100	100	80
Accounts receivable	150	150	150
Cash and cash equivalents	130	130	130

© The Institute of Chartered Accountants of India

Accounts payable	(160)	(160)	(160)
Retirement benefit obligations	(100)	-	(100)

You are required to calculate the deferred tax arising on acquisition of Entity S. Also calculate the Goodwill arising on acquisition.

Answers

1. The tax base of the asset is ₹ 60 (cost of ₹ 150 less cumulative tax depreciation of ₹ 90). To recover the carrying amount of ₹ 100, the entity must earn taxable income of ₹ 100, but will only be able to deduct tax depreciation of ₹ 60. Consequently, the entity will pay income taxes of ₹ 10 (₹ 40 at 25%) when it recovers the carrying amount of the asset. The difference between the carrying amount of ₹ 100 and the tax base of ₹ 60 is a taxable temporary difference of ₹ 40. Therefore, the entity recognises a deferred tax liability of ₹ 10 (₹ 40 at 25%) representing the income taxes that it will pay when it recovers the carrying amount of the asset.

2. A taxable temporary difference of ₹ 5 crore exists between the carrying value of the investment in XYZ at the reporting date of ₹ 4,378 crore (₹ 4,373 crore + ₹ 5 crore) and its tax base of ₹ 4,373 crore. Since a parent, by definition, controls a subsidiary, it will be able to control the reversal of this temporary difference, for example - through control of the dividend policy of the subsidiary. Therefore, deferred tax on such temporary difference is generally not provided unless it is probable that the temporary will reverse in the foreseeable future.

3. A taxable temporary difference of ₹ 50 crore therefore exists between the carrying value of the investment in PQR at the reporting date of ₹ 1,050 crore (₹ 1,000 crore + ₹ 50 crore) and its tax base of ₹ 1,000 crore. As ABC Ltd. does not completely control PQR Ltd. it is not in a position to control the dividend policy of PQR Ltd. As a result, it cannot control the reversal of this temporary difference and deferred tax is provided on temporary differences arising on investments in PQR Ltd. i.e.₹ 50 crore.

4. Calculation of the Book Value as per financial and tax purposes.

Financial Accounting: **₹ 000's**

Year	1	2	3	4	5
Gross Block	100	100	100	100	100
Accumulated Depreciation	20	40	60	80	100
Carrying Amount	80	60	40	20	0

© The Institute of Chartered Accountants of India

Tax Accounting: ₹ 000's

Year	1	2	3	4	5
Gross Block	100	100	100	100	100
Accumulated Depreciation	25	50	75	100	100
Carrying Amount	75	50	25	0	0

Calculation of DTL: ₹ 000's

Year	1	2	3	4	5
Carrying Amount	80	60	40	20	0
Tax Base	75	50	25	0	0
Difference	5	10	15	20	0
Deferred Tax Liability (Difference x 30%)	1.5	3	4.5	6	0

5. In this case there is a Deferred Tax Asset as the Tax base of assets acquired is higher by 25,000. DTA would be ₹ 7,500 (25,000 x 30%)

Journal entry:

Plant and equipment	Dr	250	
Inventory	Dr	120	
Debtors	Dr	200	
Goodwill	Dr	22.5 (30- 7.5)	
DTA	Dr	7.5	
To 9% Debentures			100
To Bank			500

6. The year-wise anticipated reversal of temporary differences is as under:

Particulars	Year ending on 31st March, 20X2	Year ending on 31st March, 20X3	Year ending on 31st March, 20X4	Year ending on 31st March, 20X5
Reversal of taxable temporary difference relating to accelerated depreciation over next 3 years (₹ 9,000/3)	3,000	3,000	3,000	Nil
Reversal of deductible temporary				

© The Institute of Chartered Accountants of India

difference relating to preliminary expenses over next 4 years (₹ 4,000/4)	1,000	1,000	1,000	1,000

B Limited will recognise a deferred tax liability of ₹ 2,700 on taxable temporary difference relating to accelerated depreciation of ₹ 9,000 @ 30%.

However, it will limit and recognise a deferred tax asset on reversal of deductible temporary difference relating to preliminary expenses reversing up to year ending 31st March, 20X4 amounting to ₹ 900 (₹ 3,000 @ 30%). No deferred tax asset shall be recognized for the reversal of deductible temporary difference for the year ending on 31st March, 20X5 as there are no taxable temporary differences. Further, the outlook is also a loss. However, if there are tax planning opportunities that could be identified for the year ending on 31st March, 20X5 deferred tax asset on the remainder of ₹ 1,000 (₹ 4,000 – ₹ 3,000) of deductible temporary difference could be recognised at the 30% tax rate.

7. (i) The tax loss creates a potential deferred tax asset for the group since its carrying value is nil and its tax base is ₹ 30,00,000.

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

(ii) The provision creates a potential deferred tax asset for the group since its carrying value is ₹ 20,00,000 and its tax base is nil.

This deferred tax asset can be recognised because X Ltd. is expected to generate taxable profits in excess of ₹ 20,00,000 in the year to 31st March, 20X3.

The amount of the deferred tax asset will be ₹ 4,00,000 (₹ 20,00,000 x 20%).

This asset will be presented as a deduction from the deferred tax liabilities caused by the (larger) taxable temporary differences.

(iii) The development costs have a carrying value of ₹ 15,20,000 (₹ 16,00,000 – (₹ 16,00,000 x 1/5 x 3/12)).

The tax base of the development costs is nil since the relevant tax deduction has already been claimed.

The deferred tax liability will be ₹ 3,04,000 (₹ 15,20,000 x 20%). All deferred tax liabilities are shown as non-current.

(iv) The carrying value of the loan at 31st March, 20X2 is ₹ 1,07,80,000 (₹ 1,00,00,000 – ₹ 2,00,000 + (₹ 98,00,000 x 10%)).

The tax base of the loan is ₹ 1,00,00,000.

© The Institute of Chartered Accountants of India

This creates a deductible temporary difference of ₹ 7,80,000 (₹ 1,07,80,000 – ₹ 1,00,00,000) and a potential deferred tax asset of ₹ 1,56,000 (₹ 7,80,000 x 20%).

Due to the availability of taxable profits next year (see part (ii) above), this asset can be recognised as a deduction from deferred tax liabilities.

8. Impact on consolidated balance sheet of PQR Ltd. group at 31st March, 20X2

- The tax loss creates a potential deferred tax asset for the PQR Ltd. group since its carrying value is nil and its tax base is ₹ 30,00,000. However, no deferred tax asset can be recognised because there is no prospect of being able to reduce tax liabilities in the foreseeable future as no taxable profits are anticipated.
- The development costs have a carrying value of ₹ 15,20,000 (₹ 16,00,000 – (₹ 16,00,000 x 1/5 x 3/12)). The tax base of the development costs is nil since the relevant tax deduction has already been claimed. The deferred tax liability will be ₹ 4,56,000 (₹ 15,20,000 x 30%). All deferred tax liabilities are shown as non-current.
- The carrying value of the loan at 31st March, 20X2 is ₹ 1,07,80,000 (₹ 1,00,00,000 – ₹ 200,000 + (₹ 98,00,000 x 10%)). The tax base of the loan is 1,00,00,000. This creates a deductible temporary difference of ₹ 7,80,000 and a potential deferred tax asset of ₹ 2,34,000 (₹ 7,80,000 x 30%).

9. Calculation of Deductible temporary differences:

Deferred tax asset	=	₹ 80,000
Existing tax rate	=	40%
Deductible temporary differences	=	80,000/40%
	=	₹ 2,00,000

Calculation of Taxable temporary differences:

Deferred tax liability	=	₹ 60,000
Existing tax rate	=	40%
Deductible temporary differences	=	60,000 / 40%
	=	₹ 1,50,000

Of the total deferred tax asset balance of ₹ 80,000, ₹ 28,000 is recognized in OCI

Hence, Deferred tax asset balance of Profit & Loss is ₹ 80,000 - ₹ 28,000 = ₹ 52,000

Deductible temporary difference recognized in Profit & Loss is ₹ 1,30,000 (52,000 / 40%)

Deductible temporary difference recognized in OCI is ₹ 70,000 (28,000 / 40%)

The adjusted balances of the deferred tax accounts under the new tax rate are:

© The Institute of Chartered Accountants of India

Deferred tax asset		₹
Previously credited to OCI-equity	₹ 70,000 x 0.45	31,500
Previously recognised as Income	₹ 1,30,000 x 0.45	58,500
		90,000
Deferred tax liability		
Previously recognized as expense	₹ 1,50,000 x 0.45	67,500

The net adjustment to deferred tax expense is a reduction of ₹ 2,500. Of this amount, ₹ 3,500 is recognised in OCI and ₹ 1,000 is charged to P&L.

The amounts are calculated as follows:

	Carrying amount at 45%	Carrying amount at 40%	Increase (decrease) in deferred tax expense
Deferred tax assets			
Previously credited to OCI-equity	31,500	28,000	(3,500)
Previously recognised as Income	58,500	52,000	(6,500)
	90,000	80,000	(10,000)
Deferred tax liability			
Previously recognized as expense	67,500	60,000	7,500
Net adjustment			(2,500)

An alternative method of calculation is:		₹
DTA shown in OCI	₹ 70,000 x (0.45 - 0.40)	3,500
DTA shown in Profit or Loss	₹ 1,30,000 x (0.45-0.40)	6,500
DTL shown in Profit or Loss	₹ 1,50,000 x (0.45 -0.40)	7,500

Journal Entries

		₹	₹
Deferred tax asset	Dr.	3,500	
OCI –revaluation surplus			3,500
Deferred tax asset	Dr.	6,500	
Deferred tax expense			6,500

© The Institute of Chartered Accountants of India

Deferred tax expense	Dr.	7,500	
Deferred tax liability			7,500

Alternatively, a combined journal entry may be passed as follows:

		₹	₹
Deferred tax asset	Dr.	10,000	
Deferred tax expense	Dr.	1,000	
To OCI –revaluation surplus			3,500
To Deferred tax liability			7,500

10. **Calculation of Net assets acquired (excluding the effect of deferred tax liability):**

Net assets acquired	**Tax base ₹'000**	**Fair values ₹'000**
Land and buildings	500	700
Property, plant and equipment	200	270
Inventory	100	80
Accounts receivable	150	150
Cash and cash equivalents	130	130
Total assets	1,080	1,330
Accounts payable	(160)	(160)
Retirement benefit obligations	-	(100)
Net assets before deferred tax liability	920	1,070

Calculation of deferred tax arising on acquisition of entity S and goodwill

	₹ '000	**₹ '000**
Fair values of S's identifiable assets and liabilities (excluding deferred tax)		1,070
Less: Tax base		(920)
Temporary difference arising on acquisition		150
Net deferred tax liability arising on acquisition of entity S (₹ 1,50,000 @ 40%)		60
Purchase consideration		1,500

© The Institute of Chartered Accountants of India

Less: Fair values of entity S's identifiable assets and liabilities (excluding deferred tax)	1,070	
Deferred tax liability	(60)	(1,010)
Goodwill arising on acquisition		490

Note: Since, the tax base of the goodwill is nil, taxable temporary difference of ₹ 4,90,000 arises on goodwill. However, no deferred tax is recognised on the goodwill. The deferred tax on other temporary differences arising on acquisition is provided at 40% and not 30%, because taxes will be payable or recoverable in entity S's tax jurisdictions when the temporary differences will be reversed.

© The Institute of Chartered Accountants of India

FOR SHORTCUT TO IND AS WISDOM: SCAN ME!

TEST YOUR KNOWLEDGE

Questions

1. Parent P acquired 90 percent of subsidiary S some years ago. P now sells its entire investment in S for ₹ 1,500 lakhs. The net assets of S are 1,000 and the NCI in S is ₹ 100 lakhs. The cumulative exchange differences that have arisen during P's ownership are gains of ₹ 200 lakhs, resulting in P's foreign currency translation reserve in respect of S having a credit balance of ₹ 180 lakhs, while the cumulative amount of exchange differences that have been attributed to the NCI is ₹ 20 lakhs

   Calculate P's gain on disposal in its consolidated financial statements.

2. Entity A, whose functional currency is Rupees (₹), has a foreign operation, Entity B, with a Euro functional currency. Entity B issues to A perpetual debt (i.e. it has no maturity) denominated in euros with an annual interest rate of 6 per cent. The perpetual debt has no issuer call option or holder put option. Thus, contractually it is just an infinite stream of interest payments in Euros.

   Analyse in A's consolidated financial statements, whether the perpetual debt can be considered in accordance with para 15 of Ind AS 21, a monetary item "for which settlement is neither planned nor likely to occur in the foreseeable future" (i.e. part of A's net investment in B), with the exchange gains and losses on the perpetual debt therefore being recorded in equity?

3. Infotech Global Ltd. has a functional currency of USD and needs to translate its financial statements into the functional and presentation currency of Infotech Inc. (L$).

   The following balances appear in the books of Infotech Global Ltd. at the year-end prior to translation:

	USD	L$
Property, plant and equipment	50,000	

© The Institute of Chartered Accountants of India

Receivables	9,35,000	
Total assets	**9,85,000**	
Issued capital	50,000	30,055
Opening retained earnings	28,000	15,274
Profit & Loss A/c (Profit for the year)	20,000	
Accounts payable	8,40,000	
Accrued liabilities	47,000	
Total equity and liabilities	**9,85,000**	

Translate the above balances of Infotech Global Ltd. into L$ ready for consolidation by Infotech Inc. (Share capital and opening retained earnings have been pre-populated.)

Prepare a working of the cumulative balance of the foreign currency translation reserve.

Additional information:

Relevant exchange rates are:

Rate at beginning of the year L$ 1 = USD 1.22

Average rate for the year L$ 1 = USD 1.175

Rate at end of the year L$ 1 = USD 1.13

4. On 30th January, 20X1, A Ltd. purchased a machinery for $ 5,000 from USA supplier on credit basis. A Ltd.'s functional currency is Rupees. The exchange rate on the date of transaction is 1 $ = ₹ 60. The fair value of the machinery determined on 31st March, 20X1 is $ 5,500. The exchange rate on 31st March, 20X1 is 1$ = ₹ 65. The payment to overseas supplier done on 31st March 20X2 and the exchange rate on 31st March 20X2 is 1$ = ₹ 67. The fair value of the machinery remains unchanged for the year ended on 31st March 20X2. Tax rate is 30%. A Ltd. follows revaluation method in respect of Plant & Machinery.

   Pass the Journal entries for the year ended on 31st March 20X1 and year 20X2 according to Ind AS 21.

5. On 1st January, 20X2, P Ltd. purchased a machine for $ 2 lakhs. The functional currency of P Ltd. is Rupees. At that date the exchange rate was $1= ₹ 68. P Ltd. is not required to pay for this purchase until 30th June, 20X2. Rupees strengthened against the $ in the three months following purchase and by 31st March, 20X2 the exchange rate was $1 = ₹ 65. CFO of P Ltd. feels that these exchange fluctuations wouldn't affect the financial statements because P Ltd. has an asset and a liability denominated in rupees, which was initially the same amount. He also feels that P Ltd. depreciates this machine over four years so the future year-end amounts won't be the same.

© The Institute of Chartered Accountants of India

Examine the impact of this transaction on the financial statements of P Ltd. for the year ended 31st March, 20X2 as per Ind AS.

6. Supplier, A Ltd., enters into a contract with a customer, B Ltd., on 1st January, 20X2 to deliver goods in exchange for total consideration of USD 50 million and receives an upfront payment of USD 20 million on this date. The functional currency of the supplier is Rupees (₹). The goods are delivered and revenue is recognised on 31st March, 20X2. USD 30 million is received on 1st April, 20X2 in full and final settlement of the purchase consideration.

   The exchange rates on 1st January, 20X2 and 31st March, 20X2 are ₹ 72 per USD and ₹ 75 per USD respectively.

   State the date of transaction for advance consideration and recognition of revenue. Also state the amount of revenue in Rupees (₹) to be recognized on the date of recognition of revenue.

7. Global Limited, an Indian company acquired on 30th September, 20X1 70% of the share capital of Mark Limited, an entity registered as company in Germany. The functional currency of Global Limited is Rupees and its financial year end is 31st March, 20X2.

   (i) The fair value of the net assets of Mark Limited was 23 million EURO and the purchase consideration paid is 17.5 million EURO on 30th September, 20X1.

   The exchange rates as at 30th September, 20X1 was ₹ 82 / EURO and at 31st March, 20X2 was ₹ 84 / EURO.

   Determine the value at which the goodwill has to be recognised in the financial statements of Global Limited as on 31st March, 20X2, when NCI is valued at proportionate share of fair value of net assets of Mark Limited.

   (ii) Mark Limited sold goods costing 2.4 million EURO to Global Limited for 4.2 million EURO during the year ended 31st March, 20X2. The exchange rate on the date of purchase by Global Limited was ₹ 83 / EURO and on 31st March, 20X2 was ₹ 84 / EURO. The entire goods purchased from Mark Limited are unsold as on 31st March, 20X2.

   Determine the unrealised profit to be eliminated in the preparation of consolidated financial statements.

8. On 1st April, 20X1, Makers Ltd. raised a long term loan from foreign investors. The investors subscribed for 6 million Foreign Currency (FCY) loan notes at par. It incurred incremental issue costs of FCY 2,00,000. Interest of FCY 6,00,000 is payable annually on 31st March, starting from 31st March, 20X2. The loan is repayable in FCY on 31st March, 20X7 at a premium and the effective annual interest rate implicit in the loan is 12%. The appropriate measurement basis for this loan is amortised cost. Relevant exchange rates are as follows:

   - 1st April, 20X1 - FCY 1 = ₹ 2.50.

© The Institute of Chartered Accountants of India

- 31st March, 20X2 – FCY 1 = ₹ 2.75.
- Average rate for the year ended 31st Match, 20X2 – FCY 1 = ₹ 2.42. The functional currency of the group is Indian Rupee.

Advise the appropriate accounting treatment for the foreign currency loan in the books of Makers Ltd. for the financial year 20X1-20X2. Also calculate the initial measurement amount for the loan, finance cost for the year, closing balance and exchange gain / loss.

Answers

1. P's gain on disposal in its consolidated financial statements would be calculated in the following manner:

	(₹ in Lakhs)
Sale proceeds	1,500
Net assets of S	(1,000)
NCI derecognised	100
Foreign currency translation reserve	180
Gain on disposal	780

2. Yes, as per Ind AS 21 net investment in a foreign operation is the amount of the reporting entity's interest in the net assets of that operation.

As per para 15 of Ind AS 21, an entity may have a monetary item that is receivable from or payable to a foreign operation. An item for which settlement is neither planned nor likely to occur in the foreseeable future is, in substance, a part of the entity's net investment in that foreign operation. Such monetary items may include long-term receivables or loans. They do not include trade receivables or trade payables.

Analysis on the basis of above mentioned guidance

Through the origination of the perpetual debt, A has made a permanent investment in B. The interest payments are treated as interest receivable by A and interest payable by B, not as repayment of the principal debt. Hence, the fact that the interest payments are perpetual does not mean that settlement is planned or likely to occur. The perpetual debt can be considered part of A's net investment in B.

In accordance with para 15 of Ind AS 21, the foreign exchange gains and losses should be recorded in equity at the consolidated level because settlement of that perpetual debt is neither planned nor likely to occur.

© The Institute of Chartered Accountants of India

3. Translation of the balances for the purpose of consolidation

	USD	Rate	L$
Property, plant and equipment	50,000	1.13	44,248
Receivables	9,35,000	1.13	8,27,434
Total assets	**9,85,000**		**8,71,682**
Issued capital	50,000	—	30,055
Opening retained earnings	28,000	—	15,274
Profit for the year	20,000	1.175	17,021
Accounts payable	8,40,000	1.13	7,43,363
Accrued liabilities	47,000	1.13	41,593
Total equity and liabilities USD	**9,85,000**		**8,47,306**
Foreign Currency Translation Reserve (Refer WN-1)			**24,376**
Total equity and liabilities L$			**8,71,682**

Working Note

1 Cumulative balance of the FCTR

Particulars	Actual translated amount in L$	Amount (Refer WN-2)	Difference
	A	B	B-A
Issued capital	30,055	44,248	14,193
Opening retained earnings	15,274	24,779	9,505
Profit for the year	17,021	17,699	678
	62,350	**86,726**	**24,376**

2 Translated amount if the same conversion rate is applied to following items as applied on other items

			Translated amount
Issued capital	50,000	1.13	44,248
Opening retained earnings	28,000	1.13	24,779
Profit for the year	20,000	1.13	17,699
	98,000		**86,726**

© The Institute of Chartered Accountants of India

4. **Journal Entries**

Purchase of Machinery on credit basis on 30th January 20X1:

	₹	₹
Machinery A/c ($ 5,000 x ₹ 60) Dr.	3,00,000	
To Creditors-Machinery A/c		3,00,000
(Initial transaction will be recorded at exchange rate on the date of transaction)		

Exchange difference arising on translating monetary item on 31st March 20X1:

	₹	₹
Profit & Loss A/c [($ 5,000 x ₹ 65) – ($ 5,000 x ₹ 60)] Dr.	25,000	
To Creditors-Machinery A/c		25,000
Machinery A/c Dr.	30,000	
To Revaluation Surplus (OCI)		30,000
[Being Machinery revalued to USD 5,500; (₹ 60 x ($ 5,500 - $ 5,000)]		
Machinery A/c Dr.	27,500	
To Revaluation Surplus (OCI)		27,500
(Being Machinery measured at the exchange rate on 31.3.20X1 [$ 5,500 x (₹ 65 - ₹ 60)]		
Revaluation Surplus (OCI) Dr.	17,250	
To Deferred Tax Liability		17,250
(DTL created @ of 30% of the total OCI amount)		

Exchange difference arising on translating monetary item and settlement of creditors on 31st March 20X2:

	₹	₹
Creditors-Machinery A/c ($ 5,000 x ₹ 65) Dr.	3,25,000	
Profit & loss A/c [(5,000 x (₹ 67 -₹ 65)] Dr.	10,000	
To Bank A/c		3,35,000
Machinery A/c [{$ 5,500 x (₹ 67 - ₹ 65)}] Dr.	11,000	

© The Institute of Chartered Accountants of India

To Revaluation Surplus (OCI)			11,000
Revaluation Surplus (OCI)	Dr.	3,300	
To Deferred Tax Liability			3,300
(DTL created @ of 30% of the total OCI amount)			

5. As per Ind AS 21 'The Effects of Changes in Foreign Exchange Rates' the asset and liability would initially be recognised at the rate of exchange in force at the transaction date ie 1st January, 20X2. Therefore, the amount initially recognised would be ₹ 1,36,00,000 ($ 2,00,000 x ₹ 68).

The liability is a monetary item, so it is retranslated using the rate of exchange in force at 31st March, 20X2. This makes the closing liability of ₹ 1,30,00,000 ($ 2,00,000 x ₹ 65).

The gain on re-translation of ₹ 6,00,000 (₹ 1,36,00,000 – ₹ 1,30,00,000) is recognised in the Statement of profit and loss.

The machine is a non-monetary asset carried at historical cost. Therefore, it continues to be translated using the rate of ₹ 68 to $ 1.

Depreciation of ₹ 8,50,000 (₹ 1,36,00,000 x ¼ x 3/12) would be charged to profit or loss for the year ended 31st March, 20X2.

The closing balance in property, plant and equipment would be ₹ 1,27,50,000 (₹ 1,36,00,000 – ₹ 8,50,000). This would be shown as a non-current asset in the balance sheet.

6. This is the case of Revenue recognised at a single point in time with multiple payments. As per the guidance given in Appendix B to Ind AS 21:

A Ltd. will recognise a non-monetary contract liability amounting ₹ 1,440 million, by translating USD 20 million at the exchange rate on 1st January, 20X2 ie ₹ 72 per USD.

A Ltd. will recognise revenue at 31st March, 20X2 (that is, the date on which it transfers the goods to the customer).

A Ltd. determines that the date of the transaction for the revenue relating to the advance consideration of USD 20 million is 1st January, 20X2. Applying paragraph 22 of Ind AS 21, A Ltd. determines that the date of the transaction for the remainder of the revenue as 31st March, 20X2.

On 31st March, 20X2, A Ltd. will:

- derecognise the non-monetary contract liability of USD 20 million and recognise USD 20 million of revenue using the exchange rate as at 1st January, 20X2 ie ₹ 72 per USD; and

© The Institute of Chartered Accountants of India

- recognise revenue and a receivable for the remaining USD 30 million, using the exchange rate on 31st March, 20X2 ie ₹ 75 per USD.
- the receivable of USD 30 million is a monetary item, so it should be translated using the closing rate until the receivable is settled.

7. (i) Para 47 of Ind AS 21 requires that goodwill arose on business combination shall be expressed in the functional currency of the foreign operation and shall be translated at the closing rate in accordance with paragraphs 39 and 42. In this case the amount of goodwill in EURO will be as follows:

Net identifiable asset	Dr.	23 million	
Goodwill (bal. fig.)	Dr.	1.4 million	
To Bank			17.5 million
To NCI (23 x 30%)			6.9 million

Thus, goodwill on reporting date would be 1.4 million EURO x ₹ 84 =₹ 117.6 million

(ii)

Particulars	EURO in million
Sale price of Inventory	4.20
Unrealised Profit [a]	1.80

Exchange rate as on date of purchase of Inventory [b]` 83 / Euro

Unrealized profit to be eliminated [a x b]` 149.40 million

As per para 39 of Ind AS 21 "income and expenses for each statement of profit and loss presented (ie including comparatives) shall be translated at exchange rates at the dates of the transactions".

In the given case, purchase of inventory is an expense item shown in the statement profit and loss. Hence, the exchange rate on the date of purchase of inventory is taken for calculation of unrealized profit which is to be eliminated while preparation of financial statements.

8. Initial carrying amount of loan in books

Loan amount received = 60,00,000 FCY

Less: Incremental issue costs = 2,00,000 FCY

58,00,000 FCY

Ind AS 21, "The Effect of Changes in Foreign Exchange Rates" states that foreign currency transactions are initially recorded at the rate of exchange in force when the transaction was

© The Institute of Chartered Accountants of India

first recognized.

Loan to be converted in Rupees (₹) = 58,00,000 FCY x ₹ 2.50/FCY

= ₹ 1,45,00,000

Therefore, the loan would initially be recorded at ₹ 1,45,00,000.

Calculation of amortized cost of loan (in FCY) at the year end:

Period	Opening Financial Liability (FCY) A	Interest @ 12% (FCY) B	Cash Flow (FCY) C	Closing Financial Liability (FCY) A+B-C
20X1-20X2	58,00,000	6,96,000	6,00,000	58,96,000

The finance cost in FCY is 6,96,000

The finance cost would be recorded at an average rate for the period since it accrues over a period of time.

Hence, the finance cost for financial year 20X1-20X2 in Rupees (₹) is ₹ 16,84,320 (6,96,000 FCY x ₹ 2.42 / FCY)

The actual payment of interest would be recorded at 6,00,000 x 2.75 = ₹ 16,50,000

The loan balance is a monetary item, so it is translated at the rate of exchange at the reporting date.

So, the closing loan balance in Rupees (₹) is 58,96,000 FCY x ₹ 2.75 / FCY = ₹ 1,62,14,000

The exchange differences that are created by this treatment are recognized in profit and loss.

In this case, the exchange difference is

₹ [1,62,14,000 - (1,45,00,000 + 16,84,320 – 16,50,000)] = ₹ 16,79,680.

This exchange difference is taken to profit and loss.

© The Institute of Chartered Accountants of India

FOR SHORTCUT TO IND AS WISDOM: SCAN ME!

TEST YOUR KNOWLEDGE

Questions

1. Mr. X is a domestic partner of Ms. Y. Mr. X has an investment in A Limited and Ms. Y has an investment in B Limited.

   Required

   (a) Examine when can a related party relationship is established, from the perspective of A Limited's financial statements:

   (b) Examine when can related party relationship is established, from the perspective of B Limited's financial statements:

   (c) Will A Limited and B Limited be related parties if Mr. X has only significant influence over A Limited and Ms. Y also has significant influence over B Limited:

2. A Limited has both (i) joint control over B Limited and (ii) joint control or significant influence over C Limited

   Required

   (a) Examine related party relationship from the perspective of C Limited's financial statements.

   (b) Examine related party relationship from the perspective of B Limited's financial statements.

3. ABC Ltd. is a long-standing customer of XYZ Ltd. Mrs. P whose husband is a director in XYZ Ltd. purchased a controlling interest in entity ABC Ltd. on 1st June, 20X1. Sales of products from XYZ Ltd. to ABC Ltd. in the two-month period from 1st April 20X1 to 31st May 20X1 totalled ₹ 8,00,000. Following the share purchase by Mrs. P, XYZ Ltd. began to supply the products at a discount of 20% to their normal selling price and allowed ABC Ltd. three months' credit (previously ABC Ltd. was only allowed one month's credit,

© The Institute of Chartered Accountants of India

XYZ Ltd.'s normal credit policy). Sales of products from XYZ Ltd. to ABC Ltd. in the ten-month period from 1st June 20X1 to 31st March 20X2 totalled ₹ 60,00,000. On 31st March 20X2, the trade receivables of XYZ Ltd. included ₹ 18,00,000 in respect of amounts owing by ABC Ltd.

Analyse and show (where possible by quantifying amounts) how the above event would be reported in the financial statements of XYZ Ltd. for the year ended 31st March 20X2 as per Ind AS. You are required to mention the disclosure requirements as well.

4. Mr. Atul is an independent director of a company X Ltd. He plays a vital role in the Management of X Ltd. and contributes in major decision making process of the organisation. X Ltd. pays sitting fee of ₹ 2,00,000 to him for every Board of Directors' (BOD) meeting he attends. Throughout the year, X Ltd. had 5 such meetings which was attended by Mr. Atul.

   Similarly, a non-executive director, Mr. Naveen also attended 5 BOD meetings and charged ₹ 1,50,000 per meeting. The Accountant of X Ltd. believes that they being not the employees of the organisation, their fee should not be disclosed as per related party transaction in accordance with Ind AS 24.

   Examine whether the sitting fee paid to independent director and non-executive director is required to be disclosed in the financial statements prepared as per Ind AS?

5. Mr. X, is the financial controller of ABC Ltd., a listed entity which prepares consolidated financial statements in accordance with Ind AS. Mr. X has recently produced the final draft of the financial statements of ABC Ltd. for the year ended 31st March, 20X2 to the managing director Mr. Y for approval. Mr. Y, who is not an accountant, had raised following query from Mr. X after going through the draft financial statements:

   One of the notes to the financial statements gives details of purchases made by ABC Ltd. from PQR Ltd. during the period 20X1-20X2. Mr. Y owns 100% of the shares in PQR Ltd. However, he feels that there is no requirement for any disclosure to be made in ABC Ltd.'s financial statements since the transaction is carried out on normal commercial terms and is totally insignificant to ABC Ltd., as it represents less than 1% of ABC Ltd.'s purchases.

   Provide answers to the query raised by the Managing Director Mr. Y as per Ind AS.

6. Uttar Pradesh State Government holds 60% shares in PQR Limited and 55% shares in ABC Limited. PQR Limited has two subsidiaries namely P Limited and Q Limited. ABC Limited has two subsidiaries namely A Limited and B Limited. Mr. KM is one of the Key management personnel in PQR Limited.

   (a) Determine the entity to whom exemption from disclosure of related party transactions is to be given. Also examine the transactions and with whom such exemption applies.

   (b) What are the disclosure requirements for the entity which has availed the exemption?

© The Institute of Chartered Accountants of India

7. S Ltd., a wholly owned subsidiary of P Ltd is the sole distributor of electricity to consumers in a specified geographical area. A manufacturing facility of P Ltd is located in the said geographical area and, accordingly, P Ltd is also a consumer of electricity supplied by S Ltd. The electricity tariffs for the geographical area are determined by an independent rate-setting authority and are applicable to all consumers of S Ltd, including P Ltd.

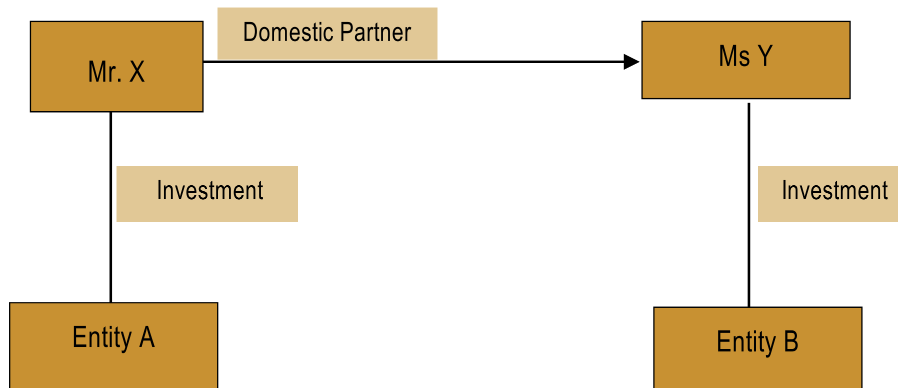
   Whether the above transaction is required to be disclosed as a related party transaction as per Ind AS 24 in the financial statements of S Ltd.? What should be the disclosures in this regard?

Answers

1. (a) If Mr. X controls or jointly controls A Limited, B Limited is related to A Limited when Ms. Y has control, joint control or significant influence over B Limited.

(b) If Mr. X controls or jointly controls A Limited, A Limited is related to B Limited when Ms. Y has control, joint control or significant influence over B Limited.

(c) No, significant influence does not lead to direct/indirect control between the A Ltd. & B Ltd. i.e., if Mr. X has significant influence (but not control or joint control) over Entity A and Ms. Y has significant influence (but not control or joint control) over Entity B, Entities A and B are not related to each other.



If Mr X is a member of the key management personnel of Entity A and Ms Y is a member of the key management personnel of Entity B, Entities A and B are not, in the absence of any other indicator of a related party relationship, related to each other.

2. (a) C Limited is related to B Limited and A Limited

(b) B Limited is related to C Limited and A Limited.

3. XYZ Ltd. would include the total revenue of ₹ 68,00,000 (₹ 60,00,000 + ₹8,00,000) from ABC Ltd. received / receivable in the year ended 31st March 20X2 within its revenue and show ₹ 18,00,000 within trade receivables at 31st March 20X2.

© The Institute of Chartered Accountants of India

Mrs. P would be regarded as a related party of XYZ Ltd. because she is a close family member of one of the key management personnel of XYZ Ltd.

From 1st June 20X1, ABC Ltd. would also be regarded as a related party of XYZ Ltd. because from that date ABC Ltd. is an entity controlled by another related party.

Because ABC Ltd. is a related party with whom XYZ Ltd. has transactions, then XYZ Ltd. should disclose:

- The nature of the related party relationship.
- The revenue of ₹ 60,00,000 from ABC Ltd. since 1st June 20X1.
- The outstanding balance of ₹ 18,00,000 at 31st March 20X2.

In the current circumstances it may well be necessary for XYZ Ltd. to also disclose the favourable terms under which the transactions are carried out.

4. As per paragraph 9 of Ind AS 24, Related Party Disclosures, "Key management personnel are those persons having authority and responsibility for planning, directing and controlling the activities of the entity, directly or indirectly, including any director (whether executive or otherwise) of that entity."

Accordingly, key management personnel (KMP) includes any director of the entity who are having authority and responsibility for planning, directing and controlling the activities of the entity. Hence, independent director Mr. Atul and non-executive director Mr. Naveen are covered under the definition of KMP in accordance with Ind AS.

Also as per paragraph 7 and 9 of Ind AS 19, 'Employee Benefits', an employee may provide services to an entity on a full-time, part-time, permanent, casual or temporary basis. For the purpose of the Standard, Employees include directors and other management personnel. So, they should not be reported as related party.

Therefore, contention of the Accountant is wrong that they are not employees of X Ltd.

Paragraph 17 of Ind AS requires disclosure about employee benefits for key management personnel. Therefore, an entity shall disclose key management personnel compensation in total i.e. disclosure of directors' fee of (₹ 10,00,000 + ₹ 7,50,000) ₹ 17,50,000 is to be made as employees benefits (under various categories).

Since short-term employee benefits are expected to be settled wholly before twelve months after the end of the annual reporting period in which the employees render the related services, the sitting fee paid to directors will fall under it (as per Ind AS 19) and is required to be disclosed in accordance with the paragraph 17 of Ind AS 24.

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

© The Institute of Chartered Accountants of India

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

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

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

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

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

6. **(a)** As per para 18 of Ind AS 24, 'Related Party Disclosures', if an entity had related party transactions during the periods covered by the financial statements, it shall disclose the nature of the related party relationship as well as information about those transactions and outstanding balances, including commitments, necessary for users to understand the potential effect of the relationship on the financial statements.

However, as per para 25 of the standard a reporting entity is exempt from the disclosure requirements in relation to related party transactions and outstanding balances, including commitments, with:

(i) a government that has control or joint control of, or significant influence over, the reporting entity; and

(ii) another entity that is a related party because the same government has control or joint control of, or significant influence over, both the reporting entity and the other entity

According to the above paras, for Entity P's financial statements, the exemption in paragraph 25 applies to:

(i) transactions with Government Uttar Pradesh State Government; and

(ii) transactions with Entities PQR and ABC and Entities Q, A and B.

Similar exemptions are available to Entities PQR, ABC, Q, A and B, with the transactions with UP State Government and other entities controlled directly or indirectly by UP State Government. However, that exemption does not apply to

© The Institute of Chartered Accountants of India

transactions with Mr. KM. Hence, the transactions with Mr. KM needs to be disclosed under related party transactions.

(b) It shall disclose the following about the transactions and related outstanding balances referred to in paragraph 25:

(a) the name of the government and the nature of its relationship with the reporting entity (ie control, joint control or significant influence);

(b) the following information in sufficient detail to enable users of the entity's financial statements to understand the effect of related party transactions on its financial statements:

(i) the nature and amount of each individually significant transaction; and

(ii) for other transactions that are collectively, but not individually, significant, a qualitative or quantitative indication of their extent.

7. As per paragraph 9(b)(i) of Ind AS 24, each parent, subsidiary and fellow subsidiary in a 'group' is related to the other members of the group. Thus, in the case under discussion, P Ltd is a related party of S Ltd from the perspective of financial statements of S Ltd.

Paragraph 11 of Ind AS 24 states as follows:

"In the context of this Standard, the following are not related parties:

(a) two entities simply because they have a director or other member of management personnel in common or because a member of key management personnel of one entity has significant influence over the other entity.

(b) two joint venturers simply because they share joint control of a joint venture.

(c) (i) providers of finance,(ii) trade unions, (iii) public utilities, and (iv) departments and agencies of a government that does not control, jointly control or significantly influence the reporting entity, simply by virtue of their normal dealings with an entity (even though they may affect the freedom of action of an entity or participate in its decision-making process).

(d) a customer, supplier, franchisor, distributor or general agent with whom an entity transacts a significant volume of business, simply by virtue of the resulting economic dependence."

Being engaged in distribution of electricity, S Ltd is a public utility. Had the only relationship between S Ltd and P Ltd been that of a supplier and a consumer of electricity, P Ltd would not have been regarded as a related party of S Ltd. However, as per the facts of the given case, this is not the only relationship between S Ltd and P Ltd. Apart from being a supplier of electricity to P Ltd., S Ltd is also a subsidiary of P Ltd; this is a relationship that is covered within the related party relationships to which the disclosure

© The Institute of Chartered Accountants of India

requirements of the standard apply. In view of the above, the supply of electricity by S Ltd to P Ltd is a related party transaction that attracts the disclosure requirements contained in paragraph 18 and other relevant requirements of the standard. This is notwithstanding the fact that P Ltd is charged the electricity tariffs determined by an independent rate-setting authority (i.e., the terms of supply to P Ltd are at par with those applicable to other consumers)

Ind AS 24 does not exempt an entity from disclosing related party transactions merely because they have been carried out on an arm's length basis.

© The Institute of Chartered Accountants of India

FOR SHORTCUT TO IND AS WISDOM: SCAN ME!

TEST YOUR KNOWLEDGE

Questions

1. ABC Ltd — 1 January 20X1 — Shares in issue 1,000,000

   31 March 20X1 — (a) Rights issue 1 for 5 at 90 paise

   (b) Fair value of shares ₹ 1 (cum-rights price)

   Calculate the number of shares for use in the EPS calculation for the calendar year.

2. | | | |
   |---|---|---|
   | 1 January | Shares in issue | 1,000,000 |
   | | 5% Convertible bonds | ₹ 100,000 |

   (terms of conversion 120 ordinary shares for ₹ 100)

   31 March Holders of ₹ 25,000 bonds converted to ordinary shares.

Profit for the year ended 31 December	₹ 200,000

   Tax rate 30%.

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

3. | | | |
   |---|---|---|
   | 1 January | Shares in issue | 1,000,000 |
   | | Profit for the year ended 31 December | ₹ 100,000 |
   | | Average fair value during period | ₹ 8 |

   The company has in issue 200,000 options to purchase equal ordinary shares

Exercise price	₹ 6

   Calculate the diluted EPS for the period.

© The Institute of Chartered Accountants of India

4. Calculate Basic EPS for period ending 20X0, 20X1 and 20X2, when

	20X0	20X1	20X2
Profit attributable to ordinary equity holders of the parent entity	₹ 1,100	₹ 1,500	₹ 1,800

Shares outstanding before rights issue	500 shares
Rights issue	One new share for each five outstanding shares
Exercise price	₹ 5.00
Date of rights issue	1 January 20X1
Last date to exercise rights	1 March 20X1
Market price of one ordinary share immediately before exercise on 1st March 20X1:	₹ 11.00
Reporting date	31 December

5. Calculate Subsidiary's and Group's Basic EPS and Diluted EPS, when

Parent:	
Profit attributable to ordinary equity holders of the parent entity	₹ 12,000 (excluding any earnings of, or dividends paid by, the subsidiary)
Ordinary shares outstanding	10,000
Instruments of subsidiary owned by the parent	800 ordinary shares
	30 warrants exercisable to purchase ordinary shares of subsidiary
	300 convertible preference shares
Subsidiary:	
Profit	₹ 5,400
Ordinary shares outstanding	1,000
Warrants	150, exercisable to purchase ordinary shares of the subsidiary
Exercise price	₹ 10
Average market price of one ordinary share	₹ 20
Convertible preference shares	400, each convertible into one ordinary share
Dividends on preference shares	₹ 1 per share
No inter-company eliminations or adjustments were necessary except for dividends.	

© The Institute of Chartered Accountants of India

Ignore income taxes. Also, ignore classification of the components of convertible financial instruments as liabilities and equity or the classification of related interest and dividends as expenses and equity as required by Ind AS 32.

6. CAB Limited is in the process of preparation of the consolidated financial statements of the group for the year ending 31st March, 20X3 and the extract of the same is as follows:

Particulars	Attributable to CAB Limited	Non-controlling interest	Total (₹ in '000)
Profit for the year	39,000	3,000	42,000
Other Comprehensive Income	5,000	Nil	5,000
Total Comprehensive Income	44,000	3,000	47,000

The long-term finance of the company comprises of the following:

(i) 20,00,00,000 equity shares at the beginning of the year and the company has issued 5,00,00,000 shares on 1st July, 20X2 at full market value.

(ii) 8,00,00,000 irredeemable preference shares. These shares were in issue for the whole of the year ended 31st March, 20X3. The dividend on these preference shares is discretionary.

(iii) ₹ 18 crores of 6% convertible debentures issued on 1st April, 20X1 and repayable on 31st March, 20X5 at par. Interest is payable annually. As an alternative to repayment at par, the holder on maturity can elect to exchange their convertible debentures for 10 crores ordinary shares in the company. On 1st April, 20X1, the prevailing market interest rate for four-year convertible debentures which had no right of conversion was 8%. Using an annual discount rate of 8%, the present value of ₹ 1 payable in four years is 0.74 and the cumulative present value of ₹ 1 payable at the end of years one to four is 3.31.

In the year ended 31st March, 20X3, CAB Limited declared an ordinary dividend of 0.10 paise per share and a dividend of 0.05 paise per share on the irredeemable preference shares.

Compute the following:

- the finance cost of convertible debentures and its closing balance as on 31st March, 20X3 to be presented in the consolidated financial statements.
- the basic and diluted earnings per share for the year ended 31st March, 20X3.

Assume that income tax is applicable to CAB Limited and its subsidiaries at 25%.

© The Institute of Chartered Accountants of India

Answers

1. Rights issue bonus fraction

	Shares	₹ per share	₹
Cum-rights	5	1	5.0
Rights	1	0.9	0.9
Ex-rights	**6**		**5.9**

Theoretical ex-rights price (5.9 / 6) = 0.9833

Bonus fraction = Cum-rights price / Theoretical ex-rights price

= 1/0.9833

	Number of shares
1 January - 31 March (1,000,000 × 3/12 × 1/.9833)	254,237
1 April - 31 December (1,200,000 × 9/12)	900,000
	1,154,237

2.

	Number of shares	Profit ₹
Profit		200,000
Ourdinary shares	1,000,000	
New shares on conversion (weighted average)		
9/12 × ₹ 25,000 / 100 × 120	22,500	-
Figures for basic EPS	1,022,500	200,000
Basic EPS is (₹ 200,000 / 1,022,500) = 0.196 per share		
Dilution adjustments		
Unconverted shares ₹ 75,000 / 100 × 120	90,000	
Interest: ₹ 75,000 × 5% × 0.7 (net of tax)		2,625
Converted shares pre conversion adjustment		
3/12 × ₹ 25,000 / 100 × 120	7,500	
Interest: [3/12 × ₹ 25,000 × 5% × 0.7]		219
	1,120,000	**202,844**

Diluted EPS is (₹ 202,844 / 1,120,000) = 0.181

© The Institute of Chartered Accountants of India

3. Diluted EPS

	Number of Shares	Profit (₹)	EPS
Basic	1,000,000	100,000	0.10
Dilution (Refer W.N.)	50,000	–	–
	1,050,000	100,000	0.095

Working Notes:

Proceeds of issue	(200,000 × ₹ 6) =	1,200,000
Number that would have been issued at Fair value	(1,200,000 / ₹ 8)=	150,000
Number actually issued		200,000
Number for "free" (200,000 – 150,000)		50,000

4. Calculation of theoretical ex-rights value per share

$$\frac{\text{Fair value of all outstanding shares before the exercise of rights + total amount received from exercise of rights}}{\text{Number of shares outstanding before exercise + number of shares issued in the exercise}}$$

$$\frac{(₹11.00 \times 500 \text{ shares}) + (₹5.00 \times 100 \text{ shares})}{500 \text{ shares} + 100 \text{ shares}}$$

Theoretical ex-rights value per share = ₹10.00

Calculation of adjustment factor

$$\frac{\text{Fair value per share before exercise of rights}}{\text{Theoretical ex-rights value per share}} \quad \frac{₹ 11.00}{₹ 10.00} = 1.10$$

Calculation of basic earnings per share

	20X0	20X1	20X2
20X0 Basic EPS as originally reported: ₹1,100 / 500 shares	₹ 2.20		
20X0 Basic EPS restated for rights: ₹1,100 / (500 shares x 1.1)	₹ 2.00		
20X1 Basic EPS including effects of rights issue: {₹1,500 / [(500 x 1.1 x 2/12) + (600x10/12)]}		₹ 2.54	
20X2 Basic EPS: ₹ 1,800 / 600 shares		₹ 3.00	

© The Institute of Chartered Accountants of India

5. Subsidiary's earnings per share

Basic EPS ₹ 5.00 calculated: $\frac{₹\ 5,400\ (a) - ₹\ 400\ (b)}{1,000\ (c)}$

Diluted EPS ₹ 3.66 calculated: $\frac{₹\ 5,400\ (d)}{(1,000 + 75\ (e) + 400(f))}$

Notes:

(a) Subsidiary's profit attributable to ordinary equity holders.

(b) Dividends paid by subsidiary on convertible preference shares.

(c) Subsidiary's ordinary shares outstanding.

(d) Subsidiary's profit attributable to ordinary equity holders (₹ 5,000) increased by ₹ 400 preference dividends for the purpose of calculating diluted earnings per share.

(e) Incremental shares from warrants, calculated: [(₹ 20 – ₹ 10) ÷ ₹ 20] × 150.

(f) Subsidiary's ordinary shares assumed outstanding from conversion of convertible preference shares, calculated: 400 convertible preference shares × conversion factor of 1.

Consolidated earnings per share

Basic EPS ₹ 1.63 calculated: $\frac{₹\ 12,000(a) + ₹\ 4,300(b)}{10,000(c)}$

Diluted EPS ₹ 1.61 calculated: $\frac{₹\ 12,000 + ₹\ 2,928(d) + ₹\ 55(e) + ₹\ 1,098(f)}{10,000}$

(a) Parent's profit attributable to ordinary equity holders of the parent entity.

(b) Portion of subsidiary's profit to be included in consolidated basic earnings per share, calculated: (800 × ₹ 5.00) + (300 × Re 1.00).

(c) Parent's ordinary shares outstanding.

(d) Parent's proportionate interest in subsidiary's earnings attributable to ordinary shares, calculated: (800 ÷ 1,000) × (1,000 shares × ₹ 3.66 per share).

(e) Parent's proportionate interest in subsidiary's earnings attributable to warrants, calculated: (30 ÷ 150) × (75 incremental shares × ₹ 3.66 per share).

© The Institute of Chartered Accountants of India

(f) Parent's proportionate interest in subsidiary's earnings attributable to convertible preference shares, calculated: (300 ÷ 400) × (400 shares from conversion × ₹ 3.66 per share).

6. Calculation of the liability and equity components on 6% Convertible debentures:

Present value of principal payable at the end of 4th year (₹ 1,80,000 thousand x 0.74)

= ₹ 1,33,200 thousand

Present value of interest payable annually for 4 years (₹ 1,80,000 thousand x 6% x 3.31)

= ₹ 35,748 thousand

Total liability component = ₹ 1,68,948 thousand

Therefore, equity component = ₹ 1,80,000 thousand – ₹ 1,68,948 thousand = ₹ 11,052 thousand

Calculation of finance cost and closing balance of 6% convertible debentures

Year	Opening balance ₹ in '000	Finance cost @ 8% ₹ in '000	Interest paid @ 6% ₹ in '000	Closing balance ₹ in '000
	a	b = a x 8%	c	d = a + b - c
31.3.20X2	1,68,948	13,515.84	10,800	1,71,663.84
31.3.20X3	1,71,663.84	13,733.11	10,800	1,74,596.95

Finance cost of convertible debentures for the year ended 31.3. 20X3 is ₹ **13,733.11 thousand** and closing balance as on 31.3. 20X3 is ₹ **1,74,596.95** thousand.

Calculation of Basic EPS **₹ in '000**

Profit for the year	39,000
Less: Dividend on preference shares (80,000 thousand x ₹ 0.05)	(4,000)
Profit attributable to equity shareholders	35,000

Weighted average number of shares = 20,00,00,000 + {5,00,00,000 x (9/12)}

= 23,75,00,000 shares or 2,37,500 thousand shares

Basic EPS = ₹ 35,000 thousand / 2,37,500 thousand shares

= ₹ 0.147

© The Institute of Chartered Accountants of India

Calculation of Diluted EPS **₹ in '000**

Profit for the year		39,000
Less: Dividend on preference shares (80,000 x 0.05)		(4,000)
		35,000
Add: Finance cost (as given in the above table)	13,733.11	
Less: Tax @ 25%	(3,433.28)	10,299.83
		45,299.83

Weighted average number of shares

= 20,00,00,000 + {5,00,00,000 x (9/12)} + 10,00,00,000

= 33,75,00,000 shares or 3,37,500 thousand shares

Diluted EPS = ₹ 45,299.83 thousand / 3,37,500 thousand shares

= ₹ 0.134

© The Institute of Chartered Accountants of India

FOR SHORTCUT TO IND AS WISDOM: SCAN ME!

TEST YOUR KNOWLEDGE

Questions

1. X Ltd. has identified 4 operating segments for which revenue data is given below:

	External Revenue (₹)	Internal Revenue (₹)	Total (₹)
Segment A	30,00,000	Nil	30,00,000
Segment B	6,50,000	Nil	6,50,000
Segment C	8,50,000	1,00,000	9,50,000
Segment D	5,00,000	49,00,000	54,00,000
Total Revenue	**50,00,000**	**50,00,000**	**1,00,00,000**

Additional information:

Segment C is a new business unit and management expect this segment to make a significant contribution to external revenue in coming years.

Which of the segments would be reportable under the criteria identified in Ind AS 108?

2. X Ltd. operates in coating industry. Its business segments comprise **Coating** (consisting of decorative, automotive, industrial paints and related activities) and **Others** (consisting of chemicals, polymers and related activities). Certain information for financial year 20X1-20X2 is given below: **(₹ in lakhs)**

Segments	External Revenue (including GST)	GST	Other operating income	Result	Asset	Liabilities
Coating	2,00,000	5,000	40,000	10,000	50,000	30,000
Others	70,000	3,000	15,000	4,000	30,000	10,000

© The Institute of Chartered Accountants of India

Additional information:

1. Unallocated income net of expenses is ₹ 30,00,00,000
2. Interest and bank charges is ₹ 20,00,00,000
3. Income tax expenses is ₹ 20,00,00,000 (current tax ₹ 19,50,00,000 and deferred tax ₹ 50,00,000)
4. Unallocated Investments are ₹ 1,00,00,00,000 and other assets are ₹ 1,00,00,00,000.
5. Unallocated liabilities, Reserves & surplus and share capital are ₹ 2,00,00,00,000, ₹ 3,00,00,00,000 & ₹ 1,00,00,00,000 respectively.
6. Depreciation amounts for coating & others are ₹ 10,00,00,000 and ₹ 3,00,00,000 respectively.
7. Capital expenditure for coating and others are ₹ 50,00,00,000 and ₹ 20,00,00,000 respectively.
8. Revenue from outside India is ₹ 6,20,00,00,000 and segment asset outside India ₹ 1,00,00,00,000.

Based on the above information, comment how X Ltd. would disclose information about reportable segment revenue, profit or loss, assets and liabilities for financial year 20X1-20X2.

3. An entity uses the weighted average cost formula to assign costs to inventories and cost of goods sold for financial reporting purposes, but the reports provided to the chief operating decision maker use the First-In, First-Out (FIFO) method for evaluating the performance of segment operations.

   State the cost formula to be used for Ind AS 108 disclosure purposes.

4. ABC Limited has 5 operating segments namely A, B, C, D and E. The profit / loss of respective segments for the year ended 31st March, 20X1 are as follows:

Segment	**Profit/(Loss) (₹ in crore)**
A	780
B	1,500
C	(2,300)
D	(4,500)
E	6,000
Total	**1,480**

© The Institute of Chartered Accountants of India

Based on the quantitative thresholds, state which of the above segments A to E would be considered as reportable segments for the year ending 31st March, 20X1.

Answers

1. Threshold amount is ₹ 10,00,000 (₹ 1,00,00,000 × 10%).

Segment A exceeds the quantitative threshold (₹ 30,00,000 > ₹ 10,00,000) and hence reportable segment.

Segment D exceeds the quantitative threshold (₹ 54,00,000 > ₹ 10,00,000) and hence reportable segment.

Segment B & C do not meet the quantitative threshold amount and may not be classified as reportable segment.

However, the total external revenue generated by these two segments A & D represent only 70% [(₹ 35,00,000 / 50,00,000) x 100] of the entity's total external revenue. If the total external revenue reported by operating segments constitutes less than 75% of the entity total revenue, additional operating segments should be identified as reportable segments until at least 75% of the revenue is included in reportable segments.

In case of X Ltd., it is given that Segment C is a new business unit and management expect this segment to make a significant contribution to external revenue in coming years. In accordance with the requirement of Ind AS 108, X Ltd. designates this start-up segment C as a reportable segment, making the total external revenue attributable to reportable segments 87% [(₹ 43,50,000/ 50,00,000) x 100] of total entity revenues.

In this situation, Segments A, C and D will be reportable segments and Segment B will be shown as other segment.

Alternatively, segment B can be considered as a reportable segment as well as it meets the definition of operating segment. If Segment B is considered as reportable segment:

External revenue reported: ₹ 30,00,000 + ₹ 6,50,000 + ₹ 5,00,000 = ₹ 41,50,000

% of Total External Revenue = ₹ 41,50,000 / ₹ 50,00,000 = 83%

Accordingly, Segments A, B and D will be reportable segments and Segment C will be shown as other segment.

2. Segment information

(A) Information about operating segment

(1) the company's operating segments comprise:

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

Others: consisting of chemicals, polymers and related activities.

© The Institute of Chartered Accountants of India

(2) Segment revenues, results and other information. (₹ in Lakhs)

	Revenue	Coating	Others	Total
1.	**External Revenue (gross)**	**2,00,000**	**70,000**	**2,70,000**
	GST	(5,000)	(3,000)	(8,000)
	Total Revenue (net)	1,95,000	67,000	2,62,000
	Other Operating Income	40,000	15,000	55,000
	Total Revenue	2,35,000	82,000	3,17,000
2.	**Results**			
	Segment results	10,000	4,000	14,000
	Unallocated income (net of unallocated expenses)			3,000
	Profit from operation before interest, taxation and exceptional items			**17,000**
	Interest and bank charges			(2,000)
	Profit before exceptional items			**15,000**
	Exceptional items			Nil
	Profit before taxation			**15,000**
	Income Taxes			
	-Current taxes			(1,950)
	-Deferred taxes			(50)
	Profit after taxation			**13,000**
3.	**Other Information**			
(a)	**Assets**			
	Segment Assets	50,000	30,000	80,000
	Investments			10,000
	Unallocated assets			10,000
	Total Assets			**1,00,000**
(b)	**Liabilities and Shareholder's funds**			
	Segment liabilities	30,000	10,000	40,000
	Unallocated liabilities			20,000
	Share capital			10,000

© The Institute of Chartered Accountants of India

	Reserves and surplus			30,000
	Total liabilities and shareholder's funds			**1,00,000**
(c)	**Others**			
	Capital Expenditure	(5,000)	(2,000)	(7,000)
	Depreciation	(1,000)	(300)	(1,300)
Geographical Information				**(₹ in lakhs)**
		India (₹)	**Outside India (₹)**	**Total (₹)**
	Revenue	2,55,000	62,000	3,17,000
	Segment assets	90,000	10,000	1,00,000
	Capital expenditure	7,000		7,000

Notes:

(i) The operating segments have been identified in line with the Ind AS 108, taking into account the nature of product, organisation structure, economic environment and internal reporting system.

(ii) Segment revenue, results, assets and liabilities include the respective amounts identifiable to each of the segments. Unallocable assets include unallocable non-current assets and other current assets. Unallocable liabilities include unallocable current liabilities and net deferred tax liability.

(iii) Corresponding figures for previous year have not been provided. However, in a practical scenario the corresponding figures would need to be given.

3. The entity should use First-in-first-out (FIFO) method for its Ind AS 108 disclosures, even though it uses the weighted average cost formula for measuring inventories for inclusion in its financial statements. Where chief operating decision maker uses only one measure of segment asset, same measure should be used to report segment information. Accordingly, in the given case, the method used in preparing the financial information for the chief operating decision maker should be used for reporting under Ind AS 108.

However, reconciliation between the segment results and results as per financial statements needs to be given by the entity in its segment report.

4. With regard to quantitative thresholds to determine reportable segment relevant in context of instant case, paragraph 13(b) of Ind AS 108 may be noted which provides as follows:

"The absolute amount of its reported profit or loss is 10 per cent or more of the greater, in absolute amount, of (i) the combined reported profit of all operating segments that did not

© The Institute of Chartered Accountants of India

report a loss and (ii) the combined reported loss of all operating segments that reported a loss."

In compliance with Ind AS 108, the segment profit/loss of respective segment will be compared with the greater of the following:

(i) All segments in profit, i.e., A, B and E – Total profit ₹ 8,280 crores.

(ii) All segments in loss, i.e., C and D – Total loss ₹ 6,800 crores.

Greater of the above – ₹ 8,280 crores.

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

Segment	Profit/(Loss) (₹ in crore)	As absolute % of ₹ 8,280 crore	Reportable segment
A	780	9%	No
B	1,500	18%	Yes
C	(2,300)	28%	Yes
D	(4,500)	54%	Yes
E	6,000	72%	Yes
Total	**1,480**		

Hence B, C, D, E are reportable segments.

© The Institute of Chartered Accountants of India

FOR SHORTCUT TO IND AS WISDOM: SCAN ME!

IND AS 32

IND AS 109

TEST YOUR KNOWLEDGE

Questions

1. As part of staff welfare measures, Y Co Ltd. has contracted to lend to its employees sums of money at 5% per annum rate of interest. The amounts lent are to be repaid in five equal instalments for principle along with the interest. The market rate of interest is 10% per annum for comparable loans. Y lent ₹ 1,600,000 to its employees on 1st January 20X1.

   Following the principles of recognition and measurement as laid down in Ind AS 109, you are required to record the entries for the year ended 31 December 20X1, for the transaction and also compute the value of loan initially to be recognised and amortised cost for all subsequent years.

   For the purpose of calculation, following discount factors at interest rate of 10% per annum may be adopted –

   At the end of year –

Year	Present value factor
1	.909
2	.827
3	.751
4	.683
5	.620

2. Wheel Co. Limited has a policy of providing subsidized loans to its employees for the purpose of buying or building houses. Mr. X, who's executive assistant to the CEO of Wheel Co. Limited, took a loan from the Company on the following terms:

© The Institute of Chartered Accountants of India

- Interest rate: 4% for the first 400,000 and 7% for the next 600,000
- Start date: 1 January 20X1
- Tenure: 5 years
- Pre-payment: Full or partial pre-payment at the option of the employee
- The principal amount of loan shall be recovered in 5 equal annual instalments and will be first applied to 7% interest bearing principal
- The accrued interest shall be paid on an annual basis
- Mr. X must remain in service till the term of the loan ends

The market rate of a comparable loan available to Mr. X, is 12% per annum.

Following table shows the contractually expected cash flows from the loan given to Mr. X:

(amount in ₹)

		Inflows			
Date	**Outflows**	**Principal**	**Interest income 7%**	**Interest income 4%**	**Principal outstanding**
1-Jan-20X1	(1,000,000)				1,000,000
31-Dec-20X1		200,000	42,000	16,000	800,000
31-Dec-20X2		200,000	28,000	16,000	600,000
31-Dec-20X3		200,000	14,000	16,000	400,000
31-Dec-20X4		200,000	-	16,000	200,000
31-Dec-20X5		200,000	-	8,000	-

Mr. S, pre-pays ₹ 200,000 on 31 December 20X2, reducing the outstanding principal as at that date to ₹ 400,000.

Following table shows the actual cash flows from the loan given to Mr. X, considering the pre-payment event on 31 December 20X2: **(amount in ₹)**

		Inflows			
Date	**Outflows**	**Principal**	**Interest income 7%**	**Interest income 4%**	**Principal outstanding**
1-Jan-20X1	(1,000,000)				1,000,000
31-Dec-20X1		200,000	42,000	16,000	800,000
31-Dec-20X2		400,000	28,000	16,000	400,000
31-Dec-20X3		200,000	-	16,000	200,000
31-Dec-20X4		200,000	-	8,000	-
31-Dec-20X5		-	-	-	-

© The Institute of Chartered Accountants of India

Record journal entries in the books of Wheel Co. Limited considering the requirements of Ind AS 109.

3. Wheel Co. Limited borrowed ₹ 500,000,000 from a bank on 1 January 20X1. The original terms of the loan were as follows:

- Interest rate: 11%
- Repayment of principal in 5 equal instalments
- Payment of interest annually on accrual basis
- Upfront processing fee: ₹ 5,870,096

Effective interest rate on loan: 11.50%

On 31 December 20X2, Wheel Co. Limited approached the bank citing liquidity issues in meeting the cash flows required for immediate instalments and re-negotiated the terms of the loan with banks as follows:

- Interest rate 15%
- Repayment of outstanding principal in 10 equal instalments starting 31 December 20X3
- Payment of interest on an annual basis

Record journal entries in the books of Wheel Co. Limited till 31 December 20X3, after giving effect of the changes in the terms of the loan on 31 December 20X2

4. K Ltd. issued 500,000, 6% convertible debentures @ ₹ 10 each on 01 April 20X1. The debentures are due for redemption on 31 March 20X5 at a premium of 10%, convertible into 2,50,000 equity shares of Rs. 10 each i.e. to the extent of 50% and balance to be settled in cash to the debenture holders. The interest rate on equivalent debentures without conversion rights was 10%.

You are required to separate the debt and equity components at the time of issue and show the accounting entries in Company's books at initial recognition. The following present values of Re 1 at 6% and at 10% are provided:

Interest rate	Year 1	Year 2	Year 3	Year 4
6%	0.94	0.89	0.84	0.79
10%	0.91	0.83	0.75	0.68

5. On 1 April 20X1, an 8% convertible loan with a nominal value of ₹ 6,00,000 was issued at par. It is redeemable on 31 March 20X5 also at par. Alternatively, it may be converted into equity shares on the basis of 100 new shares for each ₹ 200 worth of loan.

© The Institute of Chartered Accountants of India

An equivalent loan without the conversion option would have carried interest at 10%. Interest of ₹ 48,000 has already been paid and included as a finance cost.

Present value rates are as follows:

Year End	@ 8%	@ 10%
1	0.93	0.91
2	0.86	0.83
3	0.79	0.75
4	0.73	0.68

Explain how will the Company account for the above loan notes in the financial statements for the year ended 31 March 20X2?

6. On 1 April 20X1, Sun Limited guarantees a ₹ 10,00,000 loan of Subsidiary – Moon Limited, which Bank STDK has provided to Moon Limited for three years at 8%.

   Interest payments are made at the end of each year and the principal is repaid at the end of the loan term.

   If Sun Limited had not issued a guarantee, Bank STDK would have charged Moon Limited an interest rate of 11%. Sun Limited does not charge Moon Limited for providing the guarantee.

   On 31 March 20X2, there is 1% probability that Moon Limited may default on the loan in the next 12 months. If Moon Limited defaults on the loan, Sun Limited does not expect to recover any amount from Moon Limited.

   On 31 March 20X3, there is 3% probability that Moon Limited may default on the loan in the next 12 months. If Moon Limited defaults on the loan, Sun Limited does not expect to recover any amount from Moon Limited.

   Provide the accounting treatment of financial guarantee as per Ind AS 109 in the books of Sun Ltd., on initial recognition and in subsequent periods till 31 March 20X3.

© The Institute of Chartered Accountants of India

Answers

1. (i) **Calculation of initial measurement amount of loan to its employees:**

Year end	Cash flow		Total	PV factor	Present value
	Principal	Interest @ 5%			
20X1	320,000	80,000	400,000	.909	363,600
20X2	320,000	64,000	384,000	.827	317,568
20X3	320,000	48,000	368,000	.751	276,368
20X4	320,000	32,000	352,000	.683	240,416
20X5	320,000	16,000	336,000	.620	208,320
					1,406,272

(ii) **Calculation of amortised cost of loan to employees**

Year end	Amortised cost (opening balance)	Interest to be recognised	Repayment (including interest)	Amortised cost (closing balance)
20X1	1,406,272	140,627	400,000	1,146,899
20X2	1,146,899	114,690	384,000	877,589
20X3	877,589	87,759	368,000	597,348
20X4	597,348	59,735	352,000	305,083
20X5	305,083	30,917*	336,000	-

*305,083 x 10% = 30,508. Difference of ₹ 409 is due to approximation in computation.

(iii) **Journal Entries to be recorded of Y Ltd. for the year ended 31 December 20X1**

Date	Particulars	Debit	Credit
1 Jan 20X1	Staff loan A/c Dr.	14,06,272	
	Prepaid staff cost A/c* Dr. [(1,600,000 – 1,406,272), Refer part (ii)]	1,93,728	
	To Bank A/c		16,00,000
	(Being disbursement of loans to staff and excess loan balance over present value thereof in order to reflect the loan at its present value booked as prepaid staff cost)		

© The Institute of Chartered Accountants of India

31 Dec 20X1	Staff loan A/c Dr.	1,40,627	
	To Interest expense A/c		1,40,627
	(Being interest accrued on loans to staff)		
31 Dec 20X1	Staff cost A/c Dr.	38,746	
	To Prepaid expense A/c		38,746
	(Being prepaid expense charged for the year against staff cost)		

* Where the difference between the amount given by the Company to its employees and its fair value represents another asset, then such asset shall be recognised. Accordingly, such difference is recognised as prepaid employee cost and amortised over the period of loan.

2. As per requirement of Ind AS 109, a financial instrument is initially measured and recorded at its fair value. Therefore, considering the market rate of interest of similar loan available to Mr. X is 12%, the fair value of the contractual cash flows shall be as follows:

	Inflows				
Date	**Principal**	**Interest income 7%**	**Interest income 4%**	**Discount factor @12%**	**PV**
31-Dec-20X1	200,000	42,000	16,000	0.8929	2,30,357
31-Dec-20X2	200,000	28,000	16,000	0.7972	1,94,515
31-Dec-20X3	200,000	14,000	16,000	0.7118	1,63,709
31-Dec-20X4	200,000	-	16,000	0.6355	1,37,272
31-Dec-20X5	200,000	-	8,000	0.5674	1,18,025
Total (fair value)					8,43,878

Benefit to Mr. X, to be considered a part of employee cost for Wheel Co. ₹ 1,56,121.

The deemed employee cost is to be amortised over the period of loan i.e. the minimum period that Mr. X must remain in service.

The amortization schedule of the ₹ 843,878 loan is shown in the following table:

Date	**Loan outstanding**	**Total cash inflows (principal repayment + interest**	**Interest @ 12%**
1-Jan-20X1	843,878		
31-Dec-20X1	687,143	258,000	101,265
31-Dec-20X2	525,600	244,000	82,457

© The Institute of Chartered Accountants of India

31-Dec-20X3	358,672	230,000	63,072
31-Dec-20X4	185,713	216,000	43,041
31-Dec-20X5	(0)	208,000	22,287*

* Difference is due to approximation.

Journal Entries to be recorded at every period end:

a. 1 January 20X1 –

Particulars		Dr. Amount (₹)	Cr. Amount (₹)
Loan to employee A/c	Dr.	843,879	
Pre-paid employee cost A/c	Dr	156,121	
To Bank A/c			1,000,000
(Being loan asset recorded at initial fair value)			

b. 31 December 20X1 –

Particulars		Dr. Amount (₹)	Cr. Amount (₹)
Bank A/c	Dr.	258,000	
To Interest income (profit and loss) @12% A/c			101,265
To Loan to employee A/c			156,735
(Being first instalment of repayment of loan accounted for using the amortised cost and effective interest rate of 12%)			
Employee benefit (profit and loss) A/c	Dr.	31,224	
To Pre-paid employee cost A/c			31,224
(Being amortization of pre-paid employee cost charged to profit and loss as employee benefit cost)			

On 31 December 20X2, due to pre-payment of a part of loan by Mr. X, the carrying value of the loan shall be re-computed by discounting the future remaining cash flows by the original effective interest rate.

There shall be two sets of accounting entries on 31 December 20X2, first the realisation of the contractual cash flow as shown in (c) below and then the accounting for the pre-payment of ₹ 200,000 included in (d) below:

© The Institute of Chartered Accountants of India

c. 31 December 20X2 –

Particulars	Dr. Amount (₹)	Cr. Amount (₹)
Bank A/c Dr.	244,000	
To Interest income (profit and loss) @12% A/c		82,457
To Loan to employee A/c		161,543
(Being second instalment of repayment of loan accounted for using the amortised cost and effective interest rate of 12%)		
Employee benefit (profit and loss) A/c Dr.	31,224	
To Pre-paid employee cost A/c		31,224
(Being amortization of pre-paid employee cost charged to profit and loss as employee benefit cost)		

Computation of new carrying value of loan to employee:

	Inflows				
Date	Principal	Interest income 7%	Interest income 4%	Discount factor @12%	PV
31-Dec-20X3	200,000	-	16,000	0.8929	192,857
31-Dec-20X4	200,000	-	8,000	0.7972	165,816
Total (revised carrying value)					358,673
Less: Current carrying value					525,601
Adjustment required					166,928

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

d. 31 December 20X2 prepayment–

Particulars	Dr. Amount (₹)	Cr. Amount (₹)
Bank A/c Dr.	200,000	
To Pre-paid employee cost A/c		33,072
To Loan to employee A/c		166,928
(Being gain to Wheel Co. Limited recorded as an adjustment to pre-paid employee cost)		

© The Institute of Chartered Accountants of India

The amortisation schedule of the new carrying amount of loan shall be as follows:

Date	Loan outstanding	Total cash inflows (principal repayment + interest	Interest @ 12%
31-Dec-20X2	358,673		
31-Dec-20X3	185,714	216,000	43,041
31-Dec-20X4	-	208,000	22,286

Amortisation of employee benefit cost shall be as follows:

Date	Balance	Amortised to P&L	Adjustment
1-Jan-20X1	156,121		
31-Dec-20X1	124,897	31,224	
31-Dec-20X2	60,601	31,224	33,072
31-Dec-20X3	30,300	30,300	
31-Dec-20X4	-	30,300	

e. 31 December 20X3 –

Particulars	Dr. Amount (₹)	Cr. Amount (₹)
Bank A/c Dr.	216,000	
To Interest income (profit and loss) @12% A/c		43,041
To Loan to employee A/c		172,959
(Being third instalment of repayment of loan accounted for using the amortised cost and effective interest rate of 12%)		
Employee benefit (profit and loss) A/c Dr	30,300	
To Pre-paid employee cost A/c		30,300
(Being amortization of pre-paid employee cost charged to profit and loss as employee benefit cost)		

f. 31 December 20X4 –

Particulars	Dr. Amount (₹)	Cr. Amount (₹)
Bank A/c Dr.	208,000	
To Interest income (profit and loss) @12% A/c		22,286
To Loan to employee A/c		185,714
(Being last instalment of repayment of loan accounted for using the amortised cost and effective interest rate of 12%)		

© The Institute of Chartered Accountants of India

Particulars	Dr.	Cr.
Employee benefit (profit and loss) A/c Dr.	30,300	
To Pre-paid employee cost A/c		30,300
(Being amortization of pre-paid employee cost charged to profit and loss as employee benefit cost)		

3. On the date of initial recognition, the effective interest rate of the loan shall be computed keeping in view the contractual cash flows and upfront processing fee paid. The following table shows the amortisation of loan based on effective interest rate:

Date	Cash flows (principal)	Cash flows (interest and fee)	Amortised cost (opening + interest – cash flows)	Interest @ EIR (11.50%)
1-Jan-20X1	(500,000,000)	5,870,096	494,129,904	
31-Dec-20X1	100,000,000	55,000,000	395,954,843	56,824,939
31-Dec-20X2	100,000,000	44,000,000	297,489,650	45,534,807
31-Dec-20X3	100,000,000	33,000,000	198,700,959	34,211,310
31-Dec-20X4	100,000,000	22,000,000	99,551,570	22,850,610
31-Dec-20X5	100,000,000	11,000,000	(0)	11,448,430

a. 1 January 20X1 –

Particulars	Dr. Amount (₹)	Cr. Amount (₹)
Bank A/c Dr.	494,129,904	
To Loan from bank A/c		494,129,904
(Being loan recorded at its fair value less transaction costs on the initial recognition date)		

b. 31 December 20X1 –

Particulars	Dr. Amount (₹)	Cr. Amount (₹)
Loan from bank A/c Dr.	98,175,061	
Interest expense (profit and loss) Dr.	56,824,939	
To Bank A/c		155,000,000
(Being first instalment of loan and payment of interest accounted for as an adjustment to the amortised cost of loan)		

© The Institute of Chartered Accountants of India

c. 31 December 20X2 – Before Wheel Co. Limited approached the bank –

Particulars	Dr. Amount (₹)	Cr. Amount (₹)
Interest expense (profit and loss) Dr.	45,534,807	
To Loan from bank A/c		1,534,807
To Bank A/c		44,000,000
(Being loan payment of interest recorded by the Company before it approached the Bank for deferment of principal)		

Upon receiving the new terms of the loan, Wheel Co. Limited, re-computed the carrying value of the loan by discounting the new cash flows with the original effective interest rate and comparing the same with the current carrying value of the loan. As per requirements of Ind AS 109, any change of more than 10% shall be considered a substantial modification, resulting in fresh accounting for the new loan:

Date	Cash flows (principal)	Interest outflow @15%	Discount factor	PV of cash flows
31-Dec-20X2	(400,000,000)			
31-Dec-20X3	40,000,000	60,000,000	0.8969	89,686,099
31-Dec-20X4	40,000,000	54,000,000	0.8044	75,609,805
31-Dec-20X5	40,000,000	48,000,000	0.7214	63,483,092
31-Dec-20X6	40,000,000	42,000,000	0.6470	53,053,542
31-Dec-20X7	40,000,000	36,000,000	0.5803	44,100,068
31-Dec-20X8	40,000,000	30,000,000	0.5204	36,429,133
31-Dec-20X9	40,000,000	24,000,000	0.4667	29,871,422
31-Dec-20Y0	40,000,000	18,000,000	0.4186	24,278,903
31-Dec-20Y1	40,000,000	12,000,000	0.3754	19,522,235
31-Dec-20Y3	40,000,000	6,000,000	0.3367	15,488,493
PV of new contractual cash flows discounted at 11.50%				451,522,791
Carrying amount of loan				397,489,650
Difference				54,033,141
Percentage of carrying amount				13.59%

Note: Calculation done above is on full decimal, though in the table discount factor is limited to 4 decimals.

© The Institute of Chartered Accountants of India

Considering a more than 10% change in PV of cash flows compared to the carrying value of the loan, the existing loan shall be considered to have been extinguished and the new loan shall be accounted for as a separate financial liability. The accounting entries for the same are included below:

d. 31 December 20X2 – accounting for extinguishment

Particulars	Dr. Amount (₹)	Cr. Amount (₹)
Loan from bank (old) A/c Dr.	397,489,650	
Loss on modification of loan (profit and loss) Dr.	2,510,350	
To Loan from bank (new) A/c		400,000,000
(Being new loan accounted for at its principal amount in absence of any transaction costs directly related to such loan and correspondingly a de-recognition of existing loan)		

e. 31 December 20X3

Particulars	Dr. Amount (₹)	Cr. Amount (₹)
Loan from bank A/c Dr.	40,000,000	
Interest expense (profit and loss) Dr.	60,000,000	
To Bank A/c		100,000,000
(Being first instalment of the new loan and payment of interest accounted for as an adjustment to the amortised cost of loan)		

4. Computation of debt component of convertible debentures on 01 April 20X1

Particulars	Amount
Present value of principal amount repayable after 4 years	
(A) 5,000,000 x 50% x 1.10 x 0.68 (10% discount factor)	1,870,000
(B) Present value of interest [300,000 x 3.17] (4 years cumulative 10% discount factor)	951,000
Total present value of debt component (A) + (B)	2,821,000
Issue proceeds from convertible debentures	5,000,000
Value of equity component	2,179,000

© The Institute of Chartered Accountants of India

Journal entry at initial recognition

Particulars	Dr. Amount (₹)	Cr. Amount (₹)
Bank A/c Dr.	5,000,000	
To 6% debenture A/c (liability component)		2,821,000
To 6% debenture A/c (equity component)		2,179,000
(Being disbursement recorded at fair value)		

5. **Step 1** There is an 'option' to convert the loans into equity i.e. the loan note holders do not have to accept equity shares; they could demand repayment in the form of cash.

Ind AS 32 states that where there is an obligation to transfer economic benefits there should be a liability recognised. On the other hand, where there is not an obligation to transfer economic benefits, a financial instrument should be recognised as equity.

In the above illustration we have both – 'equity' and 'debt' features in the instrument. There is an obligation to pay cash – i.e. interest at 8% per annum and a redemption amount – this is 'financial liability' or 'debt component'. The 'equity' part of the transaction is the option to convert. So it is a compound financial instrument.

Step 2 Debt element of the financial instrument so as to recognise the liability is the present value of interest and principal

The rate at which the same is to be discounted, is the rate of *equivalent* loan note *without* the conversion option would have carried interest at 10%, therefore this is the rate to be used for discounting

Step 3 Calculation of the debt element of the loan note as follows:

8% Interest discounted at a rate of 10% Present Value (6,00,000 x 8%)

S. No	Year	Interest amount	PVF	Amount
Year 1	20X2	48,000	0.91	43,680
Year 2	20X3	48,000	0.83	39,840
Year 3	20X4	48,000	0.75	36,063
				1,19,583
Year 4	20X5	648,000	0.68	4,40,640
Amount to be recognised as a liability				5,60,223

Initial proceeds (6,00,000)

Amount to be recognised as equity 39,777

* In year 4, the loan note is redeemed therefore ₹ 6,00,000 + ₹ 48,000 = ₹ 6,48,000.

© The Institute of Chartered Accountants of India

Step 4 The next step is to recognise the interest component equivalent to the loan that would carry if there was no option to cover. Therefore, the interest should be recognised at 10%. As on date ₹ 48,000 has been recognised in the statement of profit and loss i.e. 6,00,000 x 8% but we have discounted the present value of future interest payments and redemption amount using discount factors of 10%, so the finance charge in the statement of profit and loss must also be recognised at the same rate i.e. for the purpose of consistency.

The additional charge to be recognised in the income statement is calculated as:

Debt component of the financial instrument ₹ 5,60,000

Interest charge (5,60,000 x 10%)	₹ 56,000
Already charged to the income statement	(₹ 48,000)
Additional charge required	₹ 8,000

Journal Entries for recording additional finance cost for year ended 31 March 20X2

Particulars	Dr. Amount (₹)	Cr. Amount (₹)
Finance cost A/c Dr.	8,000	
To Debt component A/c		8,000
(Being interest recorded for difference between amount recorded earlier and that to be recorded per Ind AS 32)		

6. ***1 April 20X1***

A financial guarantee contract is initially recognised at fair value. The fair value of the guarantee will be the present value of the difference between the net contractual cash flows required under the loan, and the net contractual cash flows that would have been required without the guarantee.

Particulars	Year 1 (₹)	Year 2 (₹)	Year 3 (₹)	Total (₹)
Cash flows based on interest rate of 11% (A)	1,10,000	1,10,000	1,10,000	3,30,000
Cash flows based on interest rate of 8% (B)	80,000	80,000	80,000	2,40,000
Interest rate differential (A-B)	30,000	30,000	30,000	90,000
Discount factor @ 11%	0.901	0.812	0.731	
Interest rate differential discounted at 11%	27,030	24,360	21,930	73,320
Fair value of financial guarantee contract (at inception)				**73,320**

© The Institute of Chartered Accountants of India

Journal Entry

Particulars	Debit (₹)	Credit (₹)
Investment in subsidiary Dr.	73,320	
To Financial guarantee (liability)		73,320
(Being financial guarantee initially recorded)		

31 March 20X2

Subsequently at the end of the reporting period, financial guarantee is measured at the higher of:

- the amount of loss allowance; and
- the amount initially recognised less cumulative amortization, where appropriate.

At 31 March 20X2, there is 1% probability that Moon Limited may default on the loan in the next 12 months. If Moon Limited defaults on the loan, Sun Limited does not expect to recover any amount from Moon Limited. The 12-month expected credit losses are therefore ₹ 10,000 (Rs.10,00,000 x 1%).

The initial amount recognised less amortisation is ₹ 51,385 (₹ 73,320 + ₹ 8,065 (interest accrued based on EIR)) – ₹ 30,000 (benefit of the guarantee in year 1) Refer table below. The unwound amount is recognised as income in the books of Sun Limited, being the benefit derived by Moon Limited not defaulting on the loan during the period.

Year	Opening balance ₹	EIR @ 11%	Benefits provided ₹	Closing balance ₹
1	73,320	8,065	(30,000)	51,385
2	51,385	5,652	(30,000)	27,037
3	27,037	2,963*	(30,000)	-

* Difference is due to approximation

The carrying amount of the financial guarantee liability after amortisation is therefore ₹ 51,385, which is higher than the 12-month expected credit losses of ₹ 10,000. The liability is therefore adjusted to ₹ 51,385 (the higher of the two amounts) as follows:

Particulars	Debit (₹)	Credit (₹)
Financial guarantee (liability) Dr.	21,935	
To Profit or loss		21,935
(Being financial guarantee subsequently adjusted)		

© The Institute of Chartered Accountants of India

31 March 20X3

At 31 March 20X3, there is 3% probability that Moon Limited will default on the loan in the next 12 months. If Moon Limited defaults on the loan, Sun Limited does not expect to recover any amount from Moon Limited. The 12-month expected credit losses are therefore ₹ 30.000 (₹ 10,00,000 x 3%).

The initial amount recognised less accumulated amortisation is ₹ 27,037, which is lower than the 12-month expected credit losses (₹ 30,000). The liability is therefore adjusted to ₹ 30,000 (the higher of the two amounts) as follows:

Particulars		Debit (₹)	Credit (₹)
Financial guarantee (liability)	Dr.	21,385*	
To Profit or loss (Note)			21,385
(Being financial guarantee subsequently adjusted)			

* The carrying amount at the end of 31 March 20X2 = ₹ 51,385 less 12-month expected credit losses of ₹ 30,000.

© The Institute of Chartered Accountants of India

FOR SHORTCUT TO IND AS WISDOM: SCAN ME!

TEST YOUR KNOWLEDGE

Questions

1. Company A and Company B are in power business. Company A holds 25% of equity shares of Company B. On 1st November, Company A obtains control of Company B when it acquires a further 65% of Company B's shares, thereby resulting in a total holding of 90%. The acquisition had the following features:

    - **Consideration:** Company A transfers cash of ₹ 59,00,000 and issues 1,00,000 shares on 1st November. The market price of Company A's shares on the date of issue is ₹ 10 per share.
    - **Contingent consideration:** Company A agrees to pay additional consideration of ₹ 7,00,0g12000 if the cumulative profits of Company B exceed ₹ 70,00,000 over the next two years. At the acquisition date, it is not considered probable that the extra consideration will be paid. The fair value of the contingent consideration is determined to be ₹ 3,00,000 at the acquisition date.
    - **Transaction costs:** Company A pays acquisition-related costs of ₹ 1,00,000.
    - **Non-controlling interests (NCI):** The fair value of the NCI is determined to be ₹ 7,50,000 at the acquisition date based on market prices. Company A elects to measure non-controlling interest at fair value for this transaction.
    - **Previously held non-controlling equity interest:** Company A has owned 25% of the shares in Company B for several years. At 1st November, the investment is included in Company A's consolidated balance sheets at ₹ 6,00,000, accounted for using the equity method; the fair value is ₹ 20,00,000.

    The fair value of Company B's net identifiable assets at 1st November is ₹ 60,00,000, determined in accordance with Ind AS 103.

Determine the accounting under acquisition method for the business combination by Company A.

2. On 31st December, 20X1, Entity A issues 2.5 shares in exchange for each ordinary share of Entity B. All of Entity B's shareholders exchange their shares in Entity B. Therefore, Entity A issues 150 ordinary shares in exchange for all 60 ordinary shares of Entity B.

The fair value of each ordinary share of Entity B at 31st December, 20X1 is ₹ 40. The quoted market price of Entity A's ordinary shares at that date is ₹ 16.

The fair values of Entity A's identifiable assets and liabilities at 31st December, 20X1 are the same as their carrying amounts, except that the fair value of Entity A's non- current assets at 31st December, 20X1 is ₹ 1,500.

The balance sheets of Entity A and Entity B immediately before the business combination are:

	Entity A (legal parent, accounting acquiree)	**Entity B (legal subsidiary, accounting acquirer)**
Current assets	500	700
Non-current assets	1,300	3,000
Total assets	1,800	3,700
Current liabilities	300	600
Non-current liabilities	400	1,100
Total liabilities	700	1,700
Shareholders' equity		
Retained earnings	800	1,400
Issued equity		
100 ordinary shares	300	
60 ordinary shares		600
Total shareholders' equity	1,100	2,000
Total liabilities and shareholders' equity	1,800	3,700

Assume that Entity B's earnings for the annual period ended 31st March, 20X1 were ₹ 600 and that the consolidated earnings for the annual period ended 31st March, 20X2 were ₹ 800. Assume also that there was no change in the number of ordinary shares issued by Entity B during the annual period ended 31st March, 20X1 and during the period from 1st January, 20X1 to the date of the reverse acquisition on 31st December, 20X1.

© The Institute of Chartered Accountants of India

Calculate the fair value of the consideration transferred measure goodwill and prepare consolidated balance sheet as on 31st December, 20X1.

3. **Scenario 1: New information on the fair value of an acquired loan**

Bank F acquires Bank E in a business combination in October, 20X1. The loan by Bank E to Borrower B is recognised at its provisionally determined fair value. In December 20X1, F receives Borrower B's financial statements for the year ended 30th September, 20X1, which indicate significant decrease in Borrower B's income from operations. Basis this, the fair value of the loan to B at the acquisition date is determined to be less than the amount recognised earlier on a provisional basis.

Scenario 2: Decrease in fair value of acquired loan resulting from an event occurring during the measurement period.

Bank F acquires Bank E in a business combination in October, 20X1. The loan by Bank E to Borrower B is recognised at its provisionally determined fair value. In December 20X1, F receives information that Borrower B has lost its major customer earlier that month and this is expected to have a significant negative effect on B's operations.

Comment on the treatment done by Bank F.

4. Company A acquired 90% equity interest in Company B on 1st April, 20X1 for a consideration of ₹ 85 crores in a distress sale. Company B did not have any instrument recognised in equity. The Company appointed a registered valuer with whose assistance, the Company valued the fair value of NCI and the fair value identifiable net assets at ₹ 15 crores and ₹ 100 crores respectively.

Find the value at which NCI has to be shown in the financial statements.

5. On 1st April, 20X1, Company A acquired 5% of the equity share capital of Company B for 1,00,000. A accounts for its investment in B at Fair Value through OCI (FVOCI) under Ind AS 109, *Financial Instruments: Recognition and Measurement*. At 31st March, 20X2, A carried its investment in B at fair value and reported an unrealised gain of ₹ 5,000 in other comprehensive income, which was presented as a separate component of equity. On 1st April, 20X2, A obtains control of B by acquiring the remaining 95 percent of B.

Comment on the treatment to be done based on the facts given in the question.

6. Company A acquires 70 percent of Company S on 1st January, 20X1 for consideration transferred of ₹ 5 million. Company A intends to recognise the NCI at proportionate share of fair value of identifiable net assets. With the assistance of a suitably qualified valuation professional, A measures the identifiable net assets of B at ₹ 10 million. A performs a review and determines that the business combination did not include any transactions that should be accounted for separately from the business combination.

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

© The Institute of Chartered Accountants of India

7. Entity A and entity B provide construction services in India. Entity A is owned by a group of individuals, none of whom has control and does not have a collective control agreement. Entity B is owned by a single individual, Mr. Ram. The owners of entities A and B have decided to combine their businesses. The consideration will be settled in shares of entity B. Entity B issues new shares, amounting to 40% of its issued share capital, to its controlling shareholder, Mr. Ram. Mr. Ram then transfers the shares to the owners of entity A in exchange for their interest in entity A. At this point Mr. Ram controls both entities A and B, owning 100% of entity A and 71.42% of entity B. Mr. Ram had a controlling interest in both entity A and entity B before and after the contribution.

   Is the combination of entities A and B a combination of entities under common control?

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

   Alpha Ltd. reviewed the procedures it used to identify and measure the assets acquired and liabilities assumed and to measure the fair value of both the non controlling interest in Beta Pvt. Ltd. and the consideration transferred. After the review, it decided that the procedures and resulting measures were appropriate.

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

9. ABC Ltd. prepares consolidated financial statements upto 31st March each year. On 1st July 20X1, ABC Ltd. acquired 75% of the equity shares of JKL Ltd. and gained control of JKL Ltd. the issued shares of JKL Ltd. is 1,20,00,000 equity shares. Details of the purchase consideration are as follows:

   - On 1st July, 20X1, ABC Ltd. issued two shares for every three shares acquired in JKL Ltd. On 1st July, 20X1, the market value of an equity share in ABC Ltd. was ₹ 6.50 and the market value of an equity share in JKL Ltd. was ₹ 6.

   - On 30th June, 20X2, ABC Ltd. will make a cash payment of ₹ 71,50,000 to the former shareholders of JKL Ltd. who sold their shares to ABC Ltd. on 1st July, 20X1. On 1st July, 20X1, ABC Ltd. would have to pay interest at an annual rate of 10% on borrowings.

© The Institute of Chartered Accountants of India

- On 30th June, 20X3, ABC Ltd. may make a cash payment of ₹ 3,00,00,000 to the former shareholders of JKL Ltd. who sold their shares to ABC Ltd. on 1st July, 20X1. This payment is contingent upon the revenues of ABC Ltd. growing by 15% over the two-year period from 1st July, 20X1 to 30th June, 20X3. On 1st July, 20X1, the fair value of this contingent consideration was ₹ 2,50,00,000. On 31st March, 20X2, the fair value of the contingent consideration was ₹ 2,20,00,000.

On 1st July, 20X1, the carrying values of the identifiable net assets of JKL Ltd. in the books of that company was ₹ 6,00,00,000. On 1st July, 20X1, the fair values of these net assets was ₹ 7,00,00,000. The rate of deferred tax to apply to temporary differences is 20%.

During the nine months ended on 31st March, 20X2, JKL Ltd. had a poorer than expected operating performance. Therefore, on 31st March, 20X2 it was necessary for ABC Ltd. to recognise an impairment of the goodwill arising on acquisition of JKL Ltd., amounting to 10% of its total computed value.

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

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

On 1st April 20X1, A Ltd. acquires 100% interest in B Ltd. As per the terms of agreement the purchase consideration is payable in the following 2 tranches:

a. an immediate issuance of 10 lakhs shares of A Ltd. having face value of ₹ 10 per share;

b. a further issuance of 2 lakhs shares after one year if the profit before interest and tax of B Ltd. for the first year following acquisition exceeds ₹ 1 crore.

   i. The fair value of the shares of A Ltd. on the date of acquisition is ₹ 20 per share. Further, the management has estimated that on the date of acquisition, the fair value of contingent consideration is ₹ 25 lakhs.

   ii. During the year ended 31st March 20X2, the profit before interest and tax of B Ltd. exceeded ₹ 1 crore. As on 31st March 20X2, the fair value of shares of A Ltd. is ₹ 25 per share.

   iii. Continuing with the fact pattern in (a) above except for:

c. The number of shares to be issued after one year is not fixed.

d. Rather, A Ltd. agreed to issue variable number of shares having a fair value equal to ₹ 40 lakhs after one year, if the profit before interest and tax for the first year following acquisition exceeds ₹ 1 crore. A Ltd. issued shares with ₹ 40 lakhs after a year.

© The Institute of Chartered Accountants of India

11. As part of its business expansion strategy, KK Ltd. is in process of setting up a pharma intermediates business which is at very initial stage. For this purpose, KK Ltd. has acquired on 1st April, 20X1, 100% shares of ABR Ltd. that manufactures pharma intermediates. The purchase consideration for the same was by way of a share exchange valued at ₹ 35 crores. The fair value of ABR Ltd.' s net assets was ₹ 15 crores, but does not include:

    (i) A patent owned by ABR Ltd. for an established successful intermediate drug that has a remaining life of 8 years. A consultant has estimated the value of this patent to be ₹ 10 crores. However, the outcome of clinical trials for the same are awaited. If the trials are successful, the value of the drug would fetch the estimated ₹ 15 crores.

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

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

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

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

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

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

Particulars	Carrying value (₹ in crore)	Fair value (₹ in crore)
ASSETS:		
Non-current assets		

© The Institute of Chartered Accountants of India

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

Other information:

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

Particulars	Fair value (₹ in crore)	Remarks
Law suit filed by a customer for a claim of ₹ 2 crore	0.5	It is not probable that an outflow of resources embodying economic benefits will be required to settle the claim. Any amount which would be paid

© The Institute of Chartered Accountants of India

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

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

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

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

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

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

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

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

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

As on November, 20X6 ₹ 350 per share

As on 1st January, 20X7 ₹ 395 per share

As on 31st March, 20X7 ₹ 420 per share

On 31st May, 20X7, H Ltd. learned that certain customer relationships existing as on 1st January, 20X7, which met the recognition criteria of an intangible asset as on that date, were not considered during the accounting of business combination for the year ended 31st March, 20X7. The fair value of such customer relationships as on 1st January, 20X7

© The Institute of Chartered Accountants of India

was ₹ 3.5 crore (assume that there are no temporary differences associated with customer relations; consequently, there is no impact of income taxes on customer relations).

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

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

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

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

(a) What should be the goodwill or bargain purchase gain to be recognised by H Ltd. in its financial statements for the year ended 31st March, 20X7. For this purpose, measure non-controlling interest using proportionate share of the fair value of the identifiable net assets of S Ltd.

(b) Will the amount of non-controlling interest, goodwill, or bargain purchase gain so recognised in (a) above change subsequent to 31st March, 20X7? If yes, provide relevant journal entries.

(c) What should be the accounting treatment of the contingent consideration as on 31st March, 20X7?

13. Company X is engaged in the business of exploration & development of Oil & Gas Blocks.

Company X currently holds participating interest (PI) in below mentioned producing Block as follows:

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

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

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

© The Institute of Chartered Accountants of India

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

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

Company X is required to pay ₹ 1 Lacs against 33.33% share of PI rights owned by Company Z.

After signing of sale agreement, Operator (company Y) approach government of India for modification in PSC (Production Sharing Contract) i.e. removal of Company Z from PSC of AWM/01 and government has approved this transaction on 30.6.20X1. Government approval for the modification in PSC is essential, given the industry in which the joint operators operate.

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

Particulars	Company X		Company Z	
	31.5.20X1 ₹	30.6.20X1 ₹	31.5.20X1 ₹	30.6.20X1 ₹
Assets				
Non-Current Assets				
Property, Plant & Equipment	5,00,000	10,00,000	1,50,000	3,00,000
Right of Use Asset	1,00,000	2,00,000	10,000	20,000
Development CWIP	50,000	1,00,000	50,000	1,00,000
Financial Assets				
Loan receivable	25,000	50,000	25,000	50,000
Total Non-Current Assets	**6,75,000**	**13,50,000**	**2,35,000**	**4,70,000**
Current assets				
Inventories	1,00,000	2,00,000	15,000	30,000
Financial Assets				
Trade receivables	1,50,000	3,00,000	50,000	1,00,000
Cash and cash equivalents	2,00,000	4,00,000	1,00,000	2,00,000
Other Current Assets	2,25,000	50,000	25,000	50,000
Total Current Assets	**6,75,000**	**9,50,000**	**1,90,000**	**3,80,000**
Total Assets	**13,50,000**	**23,00,000**	**4,25,000**	**8,50,000**

© The Institute of Chartered Accountants of India

Equity and Liabilities				
Equity				
Equity share capital	3,00,000	3,00,000	1,00,000	1,00,000
Other equity	2,00,000	3,00,000	75,000	2,50,000
Total Equity	**5,00,000**	**6,00,000**	**1,75,000**	**3,50,000**
Liabilities				
Non-Current Liabilities				
Provisions	4,00,000	8,00,000	1,00,000	2,00,000
Other Liabilities	1,50,000	3,00,000	50,000	1,00,000
Total Non-Current Liabilities	**5,50,000**	**11,00,000**	**1,50,000**	**3,00,000**
Current Liabilities				
Financial Liabilities				
Trade Payables	3,00,000	6,00,000	1,00,000	2,00,000
Total Current Liabilities	**3,00,000**	**6,00,000**	**1,00,000**	**2,00,000**
Total Liabilities	**13,50,000**	**23,00,000**	**4,25,000**	**8,50,000**

Additional Information:

1. Fair Value of PPE & Development CWIP owned by Company Z as per Market participant approach is ₹ 5,00,000 & ₹ 2,00,000 respectively.
2. Fair Value of all the other assets and liabilities acquired are assumed to be at their carrying values (except cash & cash equivalent). Cash and cash equivalents of Company Z are not to be acquired by Company X as per the terms of agreement.
3. Tax rate is assumed to be 30%.
4. As per Ind AS 111, it is a joint operation whereby every operator records their share of assets and liabilities in their books.

You need to determine the following:

1. Whether the above acquisition falls under business or asset acquisition as defined under business combination standard Ind AS 103?
2. Determine the acquisition date in the above transaction?
3. Prepare Journal entries for the above-mentioned transaction?
4. Draft the Balance Sheet for Company X based on your analysis in Part 1 above as at acquisition date.

© The Institute of Chartered Accountants of India

14. Entity X acquired entity Y in a business combination as per Ind AS 103. There is an existing share-based plan in entity Y with a vesting condition for 3 years in which 2 years have already lapsed at the date of such business acquisition. Entity X agreed to replace the existing award for the employees of combined entity. The details are as below –

Acquisition date fair value of share-based payment plan	₹ 300
Number of years to vest after acquisition	1 year
Fair Value of award which replaces existing plan	₹ 400

Calculate the share-based payment values?

Answers

1. ***Identify the acquirer***

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

Determine acquisition date

As the control over the business of Company B is transferred to Company A on 1st November, that date is considered as the acquisition date.

Determine the purchase consideration

The purchase consideration in this case will comprise the following:

Cash consideration	₹ 59,00,000
Equity shares issued (1,00,000 x 10 i.e., at fair value)	₹ 10,00,000
Contingent consideration (at fair value)	₹ 3,00,000
Fair value of previously held interest	₹ 20,00,000

As such, the total purchase consideration is ₹ 92,00,000.

Acquisition cost incurred by and on behalf of the Company A for acquisition of Company B should be recognised in the Statement of profit and loss. As such, an amount of ₹ 1,00,000 should be recognised in Statement of profit and loss.

Determine fair value of identifiable assets and liabilities

The fair value of identifiable net assets is determined at ₹ 60,00,000.

© The Institute of Chartered Accountants of India

Measure NCI

The management has decided to recognise the NCI at its fair value. As such, the NCI will be recognised at ₹ 7,50,000.

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

In this case, the control has been acquired in stages i.e., before acquisition to control, the Company A exercised significant influence over Company B. As such, the previously held interest should be measured at fair value and the difference between the fair value and the carrying amount as at the acquisition date should be recognised in Statement of Profit and Loss. As such, an amount of ₹ 14,00,000 (i.e., 20,00,000 less 6,00,000) will be recognised in Statement of profit and loss.

Determination of goodwill or gain on bargain purchase

Goodwill should be calculated as follows:

	(₹)
Total consideration	92,00,000
Recognised amount of any non-controlling interest	7,50,000
Less: Fair value of Company B's net identifiable assets	(60,00,000)
Goodwill	**39,50,000**

2. Identifying the acquirer

As a result of Entity A issuing 150 ordinary shares, Entity B's shareholders own 60 per cent of the issued shares of the combined entity (i.e., 150 of the 250 total issued shares). The remaining 40 per cent are owned by Entity A's shareholders. Thus, the transaction is determined to be a reverse acquisition in which Entity B is identified as the accounting acquirer while Entity A is the legal acquirer.

Calculating the fair value of the consideration transferred

If the business combination had taken the form of Entity B issuing additional ordinary shares to Entity A's shareholders in exchange for their ordinary shares in Entity A, Entity B would have had to issue 40 shares for the ratio of ownership interest in the combined entity to be the same. Entity B's shareholders would then own 60 of the 100 issued shares of Entity B — 60 per cent of the combined entity. As a result, the fair value of the consideration effectively transferred by Entity B and the group's interest in Entity A is ₹ 1,600 (40 shares with a fair value per share of ₹ 40).

The fair value of the consideration effectively transferred should be based on the most reliable measure. Here, the quoted market price of Entity A's shares provides a more reliable basis for measuring the consideration effectively transferred than the estimated fair

© The Institute of Chartered Accountants of India

value of the shares in Entity B, and the consideration is measured using the market price of Entity A's 100 shares with a fair value per share of ₹ 16.

Measuring goodwill

Goodwill is measured as the excess of the fair value of the consideration effectively transferred (the group's interest in Entity A) over the net amount of Entity A's recognised identifiable assets and liabilities, as follows:

	₹	₹
Consideration effectively transferred		1,600
Net recognised values of Entity A's identifiable assets and liabilities		
Current assets	500	
Non-current assets	1,500	
Current liabilities	(300)	
Non-current liabilities	(400)	(1,300)
Goodwill		300

Consolidated balance sheet at 31st December, 20X1

The consolidated balance sheet immediately after the business combination is:

	₹
Non-current assets [3,000 + 1,500]	4,500
Goodwill	300
Current assets [700 + 500]	1,200
Total assets	6,000
Shareholders' equity	
Issued equity 250 ordinary shares [600 + 1,600]	2,200
Retained earnings	1,400
Total shareholders' equity	3,600
Non-current liabilities [1,100 + 400]	1,500
Current liabilities [600 + 300]	900
Total liabilities	2,400
Total liabilities and shareholders' equity	6,000

© The Institute of Chartered Accountants of India

The amount recognised as issued equity interests in the consolidated financial statements (₹ 2,200) is determined by adding the issued equity of the legal subsidiary immediately before the business combination (600) and the fair value of the consideration effectively transferred (₹ 1,600). However, the equity structure appearing in the consolidated financial statements (i.e., the number and type of equity interests issued) must reflect the equity structure of the legal parent, including the equity interests issued by the legal parent to affect the combination.

3. **Scenario 1:** The new information obtained by F subsequent to the acquisition relates to facts and circumstances that existed at the acquisition date. Accordingly, an adjustment (i.e., decrease) to in the provisional amount should be recognised for loan to B with a corresponding increase in goodwill.

Scenario 2: Basis this, the fair value of the loan to B will be less than the amount recognised earlier at the acquisition date. The new information resulting in the change in the estimated fair value of the loan to B does not relate to facts and circumstances that existed at the acquisition date, but rather is due to a new event i.e., the loss of a major customer subsequent to the acquisition date. Therefore, based on the new information, F should determine and recognise an allowance for loss on the loan in accordance with Ind AS 109, *Financial Instruments: Recognition and Measurement*, with a corresponding charge to profit or loss; goodwill is not adjusted.

4. In this case, Company A has the option to measure NCI as follows:

- Option 1: Measure NCI at fair value i.e., ₹ 15 crores as derived by the valuer;
- Option 2: Measure NCI as proportion of fair value of identifiable net assets i.e., ₹ 10 crores (100 crores x 10%)

5. At the acquisition date A recognises the gain of ₹ 5,000 in OCI as the gain or loss is not allowed to be recycled to income statement as per the requirement of Ind AS 109. A's investment in B would be at fair value and therefore does not require remeasurement as a result of the business combination. The fair value of the 5 percent investment (1,05,000) plus the fair value of the consideration for the 95 percent newly acquired interest is included in the acquisition accounting.

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

© The Institute of Chartered Accountants of India

Following that review, A concludes that the procedures followed and the resulting measurements were appropriate.

	(₹)
Identifiable net assets	1,00,00,000
Less: Consideration transferred	(50,00,000)
NCI (10 million x 30%)	(30,00,000)
Gain on bargain purchase	20,00,000

7. No. This is not a business combination of entities under common control. Mr. Ram's control of both entities before the business combination was transitory. The substance of the transaction is that entity B has obtained control of entity A. Entity B accounts for this transaction as a business combination under Ind AS 103 using acquisition accounting.

8. The amount of Beta Pvt. Ltd. identifiable net assets [₹ 400, calculated as ₹ 500 - ₹ 100) exceeds the fair value of the consideration transferred plus the fair value of the non controlling interest in Beta Pvt. Ltd. [₹ 384 calculated as 300 + 84]. Alpha Ltd. measures the gain on its purchase of the 80 per cent interest as follows:

		₹ in lakh
Amount of the identifiable net assets acquired (₹ 500 - ₹ 100)		400
Less: Fair value of the consideration transferred for Alpha Ltd. 80 per cent interest in Beta Pvt. Ltd.	300	
Add: Fair value of non controlling interest in Beta Pvt. Ltd.	84	(384)
Gain on bargain purchase of 80 per cent interest		16

Journal Entry

	₹ in lakh	₹ in lakh
Identifiable assets acquired Dr.	500	
To Cash		300
To Liabilities assumed		100
To OCI/Equity-Gain on the bargain purchase		16
To Equity-non controlling interest in Beta Pvt Ltd.		84

If the acquirer chose to measure the non controlling interest in Beta Pvt. Ltd. on the basis of its proportionate interest in the identifiable net assets of the acquire, the recognized

© The Institute of Chartered Accountants of India

amount of the non controlling interest would be ₹ 80 (₹ 400 x 0.20). The gain on the bargain purchase then would be ₹ 20 (₹ 400- (₹ 300 + ₹ 80)

9. Computation of goodwill impairment

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

Working Note:

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

10. Paragraph 37 of Ind AS 103, inter alia, provides that the consideration transferred in a business combination should be measured at fair value, which should be calculated as the sum of (a) the acquisition-date fair values of the assets transferred by the acquirer, (b) the liabilities incurred by the acquirer to former owners of the acquiree and (c) the equity interests issued by the acquirer.

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

With respect to contingent consideration, obligations of an acquirer under contingent consideration arrangements are classified as equity or a liability in accordance with

© The Institute of Chartered Accountants of India

Ind AS 32 or other applicable Ind AS, i.e., for the rare case of non-financial contingent consideration. Paragraph 40 provides that the acquirer shall classify an obligation to pay contingent consideration that meets the definition of a financial instrument as a financial liability or as equity on the basis of the definitions of an equity instrument and a financial liability in paragraph 11 of Ind AS 32, Financial Instruments: Presentation. The acquirer shall classify as an asset a right to the return of previously transferred consideration if specified conditions are met. Paragraph 58 of Ind AS 103 provides guidance on the subsequent accounting for contingent consideration.

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

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

Subsequent measurement of contingent consideration payable for business combination

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

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

(b) If the instrument will or may be settled in the issuer's own equity instruments, then it is:

(i) a non-derivative that comprises an obligation for the issuer to deliver a fixed number of its own equity instruments; or

(ii) a derivative that will be settled only by the issuer exchanging a fixed amount of cash or other financial assets for a fixed number of its own equity instruments.

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

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

© The Institute of Chartered Accountants of India

Here, the obligation to pay contingent consideration amounting to ₹ 25,00,000 is recognized as a part of equity and therefore not re-measured subsequently or on issuance of shares.

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

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

Subsequent measurement of contingent consideration payable for business combination

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

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

As at 31 March 20X2, (being the date of settlement of contingent consideration), the liability would be measured at its fair value and the resulting loss of ₹ 15,00,000 (₹ 40,00,000 – ₹ 25,00,000) should be recognized in the profit or loss for the period. A Ltd. would recognize issuance of 160,000 (`40,00,000/25) shares at a premium of ₹ 15 per share.

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

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

(i) Patent owned by ABR Ltd.: The patent owned will be recognised at fair value by KK Ltd. even though it was not recognised by ABR Ltd. in its financial statements. The patent will be amortised over the remaining useful life of the asset i.e. 8 years. Since the company is awaiting the outcome of the trials, the value of the patent cannot be estimated at ₹ 15 crore and the extra ₹ 5 crore should only be disclosed as a Contingent Asset and not recognised.

(ii) Patent internally developed by ABR Ltd.: As per para 18 of Ind AS 103 'Business Combination', the acquirer shall measure the identifiable assets acquired and the

© The Institute of Chartered Accountants of India

liabilities assumed at their acquisition date fair values. Since the patent developed has been approved for clinical use, it is an identifiable asset, hence the same will be measured at fair value ie ₹ 20 crore on the acquisition date.

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

Hence the revised working would be as follows:

	₹
Fair value of net assets of ABR Ltd.	15 crore
Add: Patent (10 + 20)	30 crore
Add: License	10 crore
Less: Grant for License	(Nil)
	55 crores
Purchase Consideration	(35 crores)
Bargain purchase	20 crore

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

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

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

© The Institute of Chartered Accountants of India

required to settle the obligation. Hence H Ltd. will recognize contingent liability of ₹ 2.5 cr.

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

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

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

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

Calculation of purchase consideration as per Ind AS 103 ₹ in crore

Investment in S Ltd.			
On 1st Nov. 20X6	15%	[(12/100) x ₹ 395 x 15%]	7.11
On 1st Jan. 20X7	45%		
Own equity given		12 x 100 x ₹ 10,000 x 45% x 1/2	270.00
Cash			50.00
Contingent consideration			22.00
			349.11

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

Item	**₹ in crore**				
	Book value	**Fair value**	**Tax base**	**Taxable (deductible) temporary difference**	**Deferred tax assets (liability) @ 30%**
Property, plant and equipment	40	90	40	50	(15)
Intangible assets	20	30	20	10	(3)
Investments	100	350	100	250	(75)

© The Institute of Chartered Accountants of India

Inventories	20	20	20	-	-
Trade receivables	20	20	20	-	-
Cash held in functional currency	4	4	4	-	-
Non-current asset held for sale	4	4	4	-	-
Indemnified asset	-	1	-	-	-
Borrowings	20	20	20	-	-
Trade payables	28	28	28	-	-
Provision for warranties	3	3	3	-	-
Current tax liabilities	4	4	4	-	-
Contingent liability		0.5	-	(0.5)	0.15
Deferred tax Liability					(92.85)

(vi) Calculation of identifiable net assets acquired

	₹ in crore	₹ in crore
Property, plant and equipment	90	
Intangible assets	30	
Investments	350	
Inventories	20	
Trade receivables	20	
Cash held in functional currency	4	
Non-current asset held for sale	4	
Indemnified asset	1	
Total asset		519
Less: Borrowings	20	
Trade payables	28	
Provision for warranties	3	
Current tax liabilities	4	
Contingent liability (2 + 0.5)	2.50	
Deferred tax liability (W.N.2)	92.85	(150.35)
Net identifiable assets		368.65

© The Institute of Chartered Accountants of India

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

Net identifiable assets of S Ltd. on 1.1.20X7 (Refer W.N.(vi)) = 368.65 crore

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

Calculation of Goodwill as per Ind AS 103

Goodwill on 1.1.20X7 = Purchase consideration + NCI – Net assets

= 349.11 + 147.46 – 368.65 = 127.92 crore

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

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

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

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

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

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

(b) .....

(c) ......; and

(d) the resulting goodwill or gain on a bargain purchase.

© The Institute of Chartered Accountants of India

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

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

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

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

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

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

Journal Entry

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

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

(c) Since the contingent considerations payable by H Ltd is not classified as equity and is within the scope of Ind AS 109 'Financial Instruments', the changes in the fair value

© The Institute of Chartered Accountants of India

shall be recognised in profit or loss. Change in Fair value of contingent consideration (23-22) ₹ 1 crore will be recognized in the Statement of Profit and Loss.

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

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

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

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

In the aforesaid transaction, Company X acquired share of participating rights owned by Company Z for the producing Block (AWM/01). The output exist in this transaction (Considering AWM/01) is a producing block. Also all the manpower and requisite facilities / machineries are owned by Joint venture and thereby all the Joint Operators. Hence, acquiring participating rights tantamount to acquire inputs (Expertise Manpower & Machinery) and it is critical to the ability to continue producing outputs. Thus, the said acquisition will fall under the Business Acquisition and hence standard Ind AS 103 is to be applied for the same.

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

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

© The Institute of Chartered Accountants of India

(3) **Journal entry for acquisition**

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

(4) **Balance Sheet of Company X as at 30.6.20X1**

(Pre & Post Acquisition of PI rights pertaining to Company Z)

Particulars	Pre-Acquisition	Adjustments	Post-Acquisition
	30.6.20X1		30.6.20X1
Assets			
Non - Current Assets			
Property Plant & Equipment	10,00,000	1,66,650	11,66,650
Right of Use Asset	2,00,000	6,666	2,06,666
Development CWIP	1,00,000	33,330	1,66,660
Financial Assets			
Loan receivable	50,000	16,665	66,665
Total Non-Current Assets	**13,50,000**		**16,06,641**

© The Institute of Chartered Accountants of India

Current assets			
Inventories	2,00,000	9,999	2,09,999
Financial Assets			
Trade receivables	3,00,000	33,330	3,33,330
Cash and cash equivalents	4,00,000	(1,00,000)	3,00,000
Other Current Assets	50,000	16,665	66,665
Total Current Assets	**9,50,000**		**9,09,994**
Total Assets	**23,00,000**		**25,16,635**
Equity and Liabilities			
Equity			
Equity share capital	3,00,000		3,00,000
Other equity	3,00,000		3,00,000
Capital Reserve (OCI)		19,988	19,988
Total Equity	**6,00,000**		**6,19,988**
Liabilities			
Non-Current Liabilities			
Provisions	8,00,000	66,660	8,66,660
Other Liabilities	3,00,000	33,330	3,33,330
Deferred Tax Liability		29,997	29,997
Total Non-Current Liabilities	**11,00,000**		**12,29,987**
Current Liabilities			
Financial liabilities			
Trade Payables	6,00,000	66,660	6,66,660
Total Current Liabilities	**6,00,000**		**6,66,660**
Total Equity and Liabilities	**23,00,000**		**25,16,635**

© The Institute of Chartered Accountants of India

Working Notes

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

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

© The Institute of Chartered Accountants of India

Note 1: Fair Value of PPE:

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

Note 2: Fair Value of Development CWIP:

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

2. Computation Goodwill/Bargain Purchase Gain

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

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

© The Institute of Chartered Accountants of India

3. **Computation of Deferred Tax Liability arising on Business Combination**

Particulars	Acquisition Date Value (₹)
Total Non - Current Assets	2,56,641
Total Current Assets (Except Cash & Cash Equivalent of ₹ 66,660)	59,994
Total Non-Current Liabilities	(99,990)
Total Current Liabilities	(66,660)
Net Assets Acquired at Fair Value	**1,49,985**
Book value of Net Assets Acquired	(49,995)
Temporary Difference	**99,990**
DTL @ 30% on Temporary Difference	**29,997**

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

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

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

14. Pre-acquisition period = 2

Post-acquisition period = 1

Total fair value at acquisition date = ₹ 300

Value to be recorded as per business combination under Ind AS 103 = ₹ 300/3 x 2 = ₹ 200

Value to be recorded as per Ind AS 102 (**A**) = ₹ 300/3 x 1 = ₹ 100

Fair value of the replacement of such award = ₹ 400

Difference from acquisition date fair value (**B**) = ₹ 400 – ₹ 300 = ₹ 100

Total value to be accounted over vesting period as per Ind AS 102 = A + B

= ₹ 100 + ₹ 100 = ₹ 200

© The Institute of Chartered Accountants of India

TEST YOUR KNOWLEDGE

Questions

1. X Limited was holding 100% of the equity share capital of Y Limited and Y Limited was treated as a subsidiary by X Limited. Now, Y Limited issues convertible preference shares to Z Limited. As per the issue document of convertible preference shares, Z Limited also gets the rights to participate in the relevant activities of Y Limited whereby Z Limited's consent is also necessary to pass any decision by the equity shareholder of Y Limited (i.e. X Limited). Determine how should X Limited account for its investment in Y Limited in its consolidated financial statements after the issue of convertible preference shares by Y Limited to Z Limited?

2. M Limited holds 90% interest in subsidiary N Limited. N Limited holds 25% interest in an associate O Limited. As at 31 March 20X1, the net assets of O Limited was ₹ 300 lakhs including profit of ₹ 40 lakhs for the year ended 31 March 20X1. Calculate how the investment in O Limited will be accounted in the consolidated financial statements of M Limited?

3. AB Limited holds 30% interest in an associate which it has acquired for a cost of ₹ 300 lakhs. On the date of acquisition of that stake, the fair value of net assets of the associate was ₹ 900 lakh. The value of goodwill on acquisition was ₹ 30 lakhs. After the acquisition, AB Limited accounted for the investment in the associate as per equity method of accounting and now the carrying value of such investment in the consolidated financial statements of AB Limited is ₹ 360 lakhs. The associate has now issued equity shares to some investors other than AB Limited for a consideration of ₹ 800 lakhs. This has effectively reduced the holding of AB Limited to 20%. Determine how AB Limited should account for such reduction in interest in the associate?

4. DEF Ltd. acquired 100% ordinary shares of ₹ 100 each of XYZ Ltd. on 1st October 20X1. On March 31, 20X2 the summarised Balance Sheets of the two companies were as given below:

	DEF Ltd.	XYZ Ltd.
Assets		
Property Plant Equipment		
Land & Buildings	15,00,000	18,00,000
Plant & Machinery	24,00,000	13,50,000
Investment in XYZ Ltd.	34,00,000	-
Inventory	12,00,000	3,64,000

© The Institute of Chartered Accountants of India

Financial Assets		
Trade Receivable	5,98,000	4,00,000
Cash	1,45,000	80,000
Total	**92,43,000**	**39,94,000**
Equity & Liabilities		
Equity Capital (Shares of ₹ 100 each fully paid)	50,00,000	20,00,000
Other Equity		
Other reserves	24,00,000	10,00,000
Retained Earnings	5,72,000	8,20,000
Financial Liabilities		
Bank Overdraft	8,00,000	-
Trade Payable	4,71,000	1,74,000
Total	**92,43,000**	**39,94,000**

The retained earnings of XYZ Ltd. showed a credit balance of ₹ 3,00,000 on 1st April 20X1 out of which a dividend of 10% was paid on 1st November; DEF Ltd. has recognised the dividend received to profit or loss account; Fair Value of P&M as on 1st October 20X1 was ₹ 20,00,000. The rate of depreciation on plant & machinery is 10%.

Following are the increases on comparison of Fair value as per respective Ind AS with Book value as on 1st October 20X1 which are to be considered while consolidating the Balance Sheets.

Liabilities	Amount	Assets	Amount
Trade Payables	1,00,000	Land & Buildings	10,00,000
		Inventories	1,50,000

Notes:

I. It may be assumed that the inventory is still unsold on balance sheet date and the Trade Payables are also not yet settled.

II. Also assume that the Other Reserves of both the companies as on 31st March 20X2 are the same as was on 1st April 20X1.

III. All fair value adjustments have not yet started impacting consolidated post-acquisition profits.

Prepare consolidated Balance Sheet as at March 31, 20X2.

© The Institute of Chartered Accountants of India

5. Ram Ltd. acquired 60% ordinary shares of ₹ 100 each of Krishan Ltd. on 1st October 20X1. On March 31, 20X2 the summarised Balance Sheets of the two companies were as given below:

	Ram Ltd.	Krishan Ltd.
Assets		
Property, Plant and Equipment		
Land & Buildings	3,00,000	3,60,000
Plant & Machinery	4,80,000	2,70,000
Investment in Krishan Ltd.	8,00,000	-
Inventory	2,40,000	72,800
Financial Assets		
Trade Receivables	1,19,600	80,000
Cash	29,000	16,000
Total	**19,68,600**	**7,98,800**
Equity & Liabilities		
Equity Capital (Shares of ₹ 100 each fully paid)	10,00,000	4,00,000
Other Equity		
Other Reserves	6,00,000	2,00,000
Retained earnings	1,14,400	1,64,000
Financial Liabilities		
Bank Overdraft	1,60,000	-
Trade Payable	94,200	34,800
Total	**19,68,600**	**7,98,800**

The Retained earnings of Krishan Ltd. showed a credit balance of ₹ 60,000 on 1st April 20X1 out of which a dividend of 10% was paid on 1st November; Ram Ltd. has credited the dividend received to its Retained earnings; Fair Value of P&M as on 1st October 20X1 was ₹ 4,00,000; The rate of depreciation on plant & machinery is 10%.

Following are the increases on comparison of Fair value as per respective Ind AS with book value as on 1st October 20X1 which are to be considered while consolidating the Balance Sheets.

© The Institute of Chartered Accountants of India

Liabilities	Amount	Assets	Amount
Trade Payables	20,000	Land & Buildings	2,00,000
		Inventories	30,000

Notes:

I. It may be assumed that the inventory is still unsold on balance sheet date and the Trade Payables are also not yet settled.

II. Also assume that the Other Reserves as on 31st March 20X2 are the same as was on 1st April 20X1.

Prepare consolidated Balance Sheet as at March 31, 20X2.

6. On 31 March 20X2, Blue Heavens Ltd. acquired 100% ordinary shares carrying voting rights of Orange County Ltd. for ₹ 6,000 lakh in cash and it controlled Orange County Ltd. from that date. The acquisition-date statements of financial position of Blue Heavens Ltd. and Orange County Ltd. and the fair values of the assets and liabilities recognised on Orange County Ltd. balance sheet were:

	Blue Heavens Ltd.	Orange County Ltd.	
	Carrying Amount (₹ in lakh)	Carrying Amount (₹ in lakh)	Fair Value (₹ in lakh)
Assets			
Non-current assets			
Building and other PPE	7,000	3,000	3,300
Investment in Orange County Ltd.	6,000		
Current assets			
Inventories	700	500	600
Trade receivables	300	250	250
Cash	1,500	700	700
Total assets	**15,500**	**4,450**	
Equity and liabilities			
Equity			
Share capital	5,000	2,000	
Retained earnings	10,200	2,300	
Current liabilities			
Trade payables	300	150	150
Total liabilities and equity	**15,500**	**4,450**	

© The Institute of Chartered Accountants of India

Prepare the Consolidated Balance Sheet as at March 31, 20X2 of group of entities Blue Heavens Ltd. and Orange County Ltd.

7. The facts are the same as in Question 6 above. However, Blue Heavens Ltd. acquires only 75% of the ordinary shares, to which voting rights are attached of Orange County Ltd. Blue Heavens Ltd. pays ₹ 4,500 lakhs for the shares. Prepare the Consolidated Balance Sheet as at March 31, 20X2 of group of entities Blue Heavens Ltd. and Orange County Ltd.

8. Facts are same as in Question 6 &7, Blue Heavens Ltd. acquires 75% of Orange County Ltd. Blue Heavens Ltd. pays ₹ 4,500 lakhs for the shares. At 31 March 20X3, i.e one year after Blue Heavens Ltd. acquired Orange County Ltd., the individual statements of financial position and statements of comprehensive income of Blue Heavens Ltd. and Orange County Ltd. are:

	Blue Heavens Ltd. Carrying Amount (₹ in lakh)	Orange County Ltd. Carrying Amount (₹ in lakh)
Assets		
Non-current assets		
PPE (Building and others)	6,500	2,750
Investment in Orange County Ltd.	4,500	
	11,000	2,750
Current assets		
Inventories	800	550
Financial Asset - Trade receivables	380	300
Cash	4,170	1,420
	5,350	2,270
Total assets	**16,350**	**5,020**
Equity and liabilities		
Equity		
Share capital	5,000	2,000
Retained earnings	11,000	2,850
	16,000	4,850

© The Institute of Chartered Accountants of India

Current liabilities		
Financial Liabilities-Trade payables	350	170
	350	170
Total liabilities and equity	**16,350**	**5,020**

Statements of Profit and Loss for the year ended 31 March 20X3:

	Blue Heavens Ltd. Carrying Amount (₹ in lakh)	Orange County Ltd. Carrying Amount (₹ in lakh)
Revenue	3,000	1,900
Cost of sales	(1,800)	(1,000)
Administrative expenses	(400)	(350)
Profit for the year	**800**	**550**

Note: Blue Heavens Ltd. estimates that goodwill has impaired by 98. The fair value adjustment to buildings and other PPE is in respect of a building; all buildings have an estimated remaining useful life of 20 years from 31 March 20X2 and estimated residual values of zero. Blue Heavens Ltd. uses the straight-line method for depreciation of PPE. All the inventory held by Orange County Ltd. at 31 March 20X2 was sold during 20X3.

Prepare the Consolidated Balance Sheet as at March 31, 20X3 of group of entities Blue Heavens Ltd. and Orange County Ltd.

9. P Pvt. Ltd. has a number of wholly-owned subsidiaries including S Pvt. Ltd. at 31st March 20X2. P Pvt. Ltd.'s consolidated balance sheet and the group carrying amount of S Pvt. Ltd.'s assets and liabilities (ie the amount included in the consolidated balance sheet in respect of S Pvt. Ltd.'s assets and liabilities) at 31st March 20X2 are as follows:

Particulars	Consolidated (₹ in millions)	Group carrying amount of S Pvt. Ltd. asset and liabilities Ltd. (₹ in millions)
Assets		
Non-Current Assets		
Goodwill	380	180
Buildings	3,240	1,340
Current Assets		

© The Institute of Chartered Accountants of India

Inventories	140	40
Trade Receivables	1,700	900
Cash	3,100	1000
Total Assets	**8,560**	**3,460**
Equities & Liabilities		
Equity		
Share Capital	1600	
Other Equity		
Retained Earnings	4,260	
Current liabilities		
Trade Payables	2,700	900
Total Equity & Liabilities	**8,560**	**900**

Prepare consolidated Balance Sheet after disposal as at 31st March, 20X2 when P Pvt. Ltd. group sold 100% shares of S Pvt. Ltd. to independent party for ₹ 3,000 millions.

10. Reliance Ltd. has a number of wholly-owned subsidiaries including Reliance Jio Infocomm Ltd. at 31st March 20X2.

    Reliance Ltd.'s consolidated balance sheet and the group carrying amount of Reliance Jio Infocomm Ltd. assets and liabilities (ie the amount included in that consolidated balance sheet in respect of Reliance Jio Infocomm Ltd. assets and liabilities) at 31st March 20X2 are as follows:

Particulars	**Consolidated (₹ In '000)**	**Group carrying amount of Reliance Jio Infocomm Ltd. asset and liabilities Ltd. (₹ In '000)**
Assets		
Non-current Assets		
Goodwill	190	90
Buildings	1,620	670
Current Assets		
Inventories	70	20

© The Institute of Chartered Accountants of India

Financial Assets		
Trade Receivables	850	450
Cash	1,550	500
Total Assets	**4,280**	**1,730**
Equity & Liabilities		
Equity		
Share Capital	800	
Other Equity		
Retained Earnings	2,130	
	2,930	
Current liabilities		
Financial liabilities		
Trade Payables	1,350	450
Total Equity & Liabilities	**4,280**	**450**

Prepare consolidated Balance Sheet after disposal as at 31st March, 20X2 when Reliance Ltd. group sold 90% shares of Reliance Jio Infocomm Ltd. to independent party for ₹ 1000 thousand.

11. Airtel Telecommunications Ltd. owns 100% share capital of Airtel Infrastructures Pvt. Ltd. On 1 April 20X1 Airtel Telecommunications Ltd. acquired a building from Airtel Infrastructures Pvt. Ltd., for ₹ 11,00,000 that the group plans to use it as its new headquarters office.

    Airtel Infrastructures Pvt. Ltd. had purchased the building from a third party on 1 April 20X0 for ₹ 10,25,000. At that time the building was assessed to have a useful life of 21 years and a residual value of ₹ 5,00,000. On 1 April 20X1 the carrying amount of the building was ₹ 10,00,000 in Airtel Infrastructures Pvt. Ltd.'s individual accounting records.

    The estimated remaining useful life of the building measured from 1 April 20X1 is 20 years and the residual value of the building is now estimated at ₹ 3,50,000. The method of depreciation is straight-line.

    Pass necessary accounting entries in individual and consolidation situations.

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

© The Institute of Chartered Accountants of India

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

These net assets include the following:

(a) Debt investments classified as fair value through other comprehensive income (FVOCI) of ₹ 12 crore and related FVOCI reserve of ₹ 6 crore.

(b) Net defined benefit liability of ₹ 6 crore that has resulted in a reserve relating to net measurement losses of ₹ 3 crore.

(c) Equity investments (considered not held for trading) of ₹ 10 crore for which irrevocable option of recognising the changes in fair value in OCI has been availed and related FVOCI reserve of ₹ 4 crore.

(d) Net assets of a foreign operation of ₹ 20 crore and related foreign currency translation reserve of ₹ 8 crore.

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

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

13. On 1st April 2019, Investor Ltd. acquires 35% interest in another entity, XYZ Ltd. Investor Ltd. determines that it is able to exercise significant influence over XYZ Ltd. Investor Ltd. has paid total consideration of ₹ 47,50,000 for acquisition of its interest in XYZ Ltd. At the date of acquisition, the book value of XYZ Ltd.'s net assets was ₹ 90,00,000 and their fair value was ₹ 1,10,00,000. Investor Ltd. has determined that the difference of ₹ 20,00,000 pertains to an item of property, plant and equipment (PPE) which has remaining useful life of 10 years.

    During the year, XYZ Ltd. made a profit of ₹ 8,00,000. XYZ Ltd. paid a dividend of ₹ 12,00,000 on 31st March, 2020. XYZ Ltd. also holds a long-term investment in equity securities. Under Ind AS, investment is classified as at FVTOCI in accordance with Ind AS 109 and XYZ Ltd. recognized an increase in value of investment by ₹ 2,00,000 in OCI during the year. Ignore deferred tax implications, if any.

    Calculate the closing balance of Investor Ltd.'s investment in XYZ Ltd. as at 31st March, 2020 as per the relevant Ind AS.

14. On 1st April 20X1 Alpha Ltd. commenced joint construction of a property with Gama Ltd. For this purpose, an agreement has been entered into that provides for joint operation and ownership of the property. All the ongoing expenditure, comprising maintenance plus borrowing costs, is to be shared equally. The construction was completed on 30th September

© The Institute of Chartered Accountants of India

20X1 and utilisation of the property started on 1st January 20X2 at which time the estimated useful life of the same was estimated to be 20 years.

Total cost of the construction of the property was ₹ 40 crores. Besides internal accruals, the cost was partly funded by way of loan of ₹ 10 crores taken on 1st January 20X1. The loan carries interest at an annual rate of 10% with interest payable at the end of year on 31st December each year. The company has spent ₹ 4,00,000 on the maintenance of such property.

The company has recorded the entire amount paid as investment in Joint Venture in the books of accounts. Suggest the suitable accounting treatment of the above transaction as per applicable Ind AS.

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

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

Firstly, Gamma Limited wants you to suggest whether GD Limited can avail the exemption from the preparation and presentation of consolidated financial statements as per applicable Ind AS?

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

Answers

1. As per the issue document of convertible preference shares, unanimous consent of both X Limited and Z Limited are required to pass any decision about the relevant activities of Y Limited. Hence, Y Limited is jointly controlled by X Limited and Z Limited and thereby, Y Limited becomes a joint arrangement between X Limited and Z Limited.

Y Limited is structured through a separate vehicle. The legal form of Y Limited, terms of the contractual arrangement or other facts and circumstances do not give X Limited and Z Limited rights to the assets, and obligations for the liabilities, relating to Y Limited. Hence, Y Limited is a joint venture between X Limited and Z Limited.

When the convertible preference shares are issued to Z Limited, X Limited losses control over Y Limited. Hence X Limited should derecognise the assets and liabilities of Y Limited from its consolidated financial statements. 100% equity shares in Y Limited is still held by X Limited. Hence such investment would be accounted at fair value on the date of loss of

© The Institute of Chartered Accountants of India

control by X Limited. The difference between the fair value of 100% equity shares retained in Y Limited and the carrying value of assets and liabilities of Y Limited derecognised is recognised in profit or loss of X Limited. After the loss of control, the investment in Y Limited is accounted as per equity method of accounting by X Limited whereby the investment value in Y Limited will be adjusted for the change in the X Limited's share of the net assets Y Limited post the date of loss of control. Also, the difference between the fair value of investment in Y Limited and fair value of net identifiable assets of Y Limited shall be goodwill or capital reserve.

2. Since N Limited is a subsidiary of M Limited, the consolidated financial statements of M Limited will include 100% amounts of the consolidated financial statements of N Limited (including investment in O Limited accounted for using equity method). Accordingly, the investment in O Limited will be accounted as follows in the consolidated financial statements of M Limited:

		₹' lakh
Investment in O Limited (300 x 25%)		75
Share in profit of O Limited		
Attributable to M Limited (40 x 25% x 90%)	9	
Attributable to Non-controlling interest of N Limited (50 x 25% x 10%)	1	10

3. Because of the issue of shares by associate to other investors, AB Limited has effectively sold 10% (30 – 20) of its interest in the associate. The gain / loss on reduction in interest in associate in calculated as follows:

	₹' lakhs
AB Limited's share in the consideration received by the associate for issue of shares (800 x 20%) (1)	160
Less: Carrying value of interest sold (360 x 1/3)(2)	(120)
Gain on reduction in interest in associate(3)	**40**

Notes:

(1) The share in the consideration received by associate on issue of shares (i.e. ₹ 160 lakhs) would be recorded as part of investment in associate.

(2) The carrying amount of interest sold (i.e. ₹ 120 lakhs) will be derecognised, including proportionate goodwill of ₹ 10 lakhs (30 x 1/3).

(3) Gain of ₹ 40 lakhs will be recorded in the profit or loss.

© The Institute of Chartered Accountants of India

4. **Consolidated Balance Sheet of DEF Ltd. and its subsidiary, XYZ Ltd. as at 31st March, 20X2**

Particulars	Note No.	₹
I. Assets		
(1) Non-current assets		
(i) Property Plant & Equipment	1	86,00,000
(2) Current Assets		
(i) Inventories	2	17,14,000
(ii) Financial Assets		
(a) Trade Receivables	3	9,98,000
(b) Cash & Cash equivalents	4	2,25,000
Total Assets		**1,15,37,000**
II. Equity and Liabilities		
(1) Equity		
(i) Equity Share Capital	5	50,00,000
(ii) Other Equity	6	49,92,000
(2) Current Liabilities		
(i) Financial Liabilities		
(a) Trade Payables	7	7,45,000
(b) Short term borrowings	8	8,00,000
Total Equity & Liabilities		**1,15,37,000**

Notes to Accounts

			₹
1.	**Property Plant & Equipment**		
	Land & Building	43,00,000	
	Plant & Machinery	43,00,000	86,00,000
2.	**Inventories**		
	DEF Ltd.	12,00,000	
	XYZ Ltd.	5,14,000	17,14,000

© The Institute of Chartered Accountants of India

3.	**Trade Receivables**		
	DEF Ltd.	5,98,000	
	XYZ Ltd.	4,00,000	9,98,000
4.	**Cash & Cash equivalents**		
	DEF Ltd.	1,45,000	
	XYZ Ltd.	80,000	2,25,000
7.	**Trade payable**		
	DEF Ltd.	4,71,000	
	XYZ Ltd.	2,74,000	7,45,000
8.	**Shorter-term borrowings**		
	Bank overdraft		8,00,000

Statement of Changes in Equity:

5. Equity share Capital

Balance at the beginning of the reporting period	Changes in Equity share capital during the year	Balance at the end of the reporting period
50,00,000	0	50,00,000

6. Other Equity

	Share application money pending allotment	Equity component of compound financial instrument	Reserves & Surplus			Total
			Capital reserve	Retained Earnings	Other Reserves	
Balance at the beginning				0	24,00,000	24,00,000
Total comprehensive income for the year			0	5,72,000		5,72,000
Dividends			0	(2,00,000)		(2,00,000)
Total						

© The Institute of Chartered Accountants of India

comprehensive income attributable to parent			0	3,35,000		3,35,000
Gain on Bargain purchase			18,85,000			18,85,000
Balance at the end of reporting period			18,85,000	7,07,000	24,00,000	49,92,000

It is assumed that there exists no clear evidence for classifying the acquisition of the subsidiary as a bargain purchase and, hence, the bargain purchase gain has been recognized directly in capital reserve. If, however, there exists such a clear evidence, the bargain purchase gain would be recognized in other comprehensive income and then accumulated in capital reserve. In both the cases, closing balance of capital reserve will be ₹ 18,85,000.

Working Notes:

1. **Adjustments of Fair Value**

The Plant & Machinery of XYZ Ltd. would stand in the books at ₹ 14,25,000 on 1st October, 20X1, considering only six months' depreciation on ₹ 15,00,000 total depreciation being ₹ 1,50,000. The value put on the assets being ₹ 20,00,000 there is an appreciation to the extent of ₹ 5,75,000.

2. **Acquisition date profits of XYZ Ltd.** ₹

Reserves on 1.4. 20X1	10,00,000
Profit & Loss Account Balance on 1.4. 20X1 Profit for 20X2: Total ₹ 8,20,000 less ₹ 1,00,000 (3,00,000 – 2,00,000) i.e. ₹ 7,20,000; for 6 months i.e. up to 1.10.20X1	3,00,000
Total Appreciation including machinery appreciation (10,00,000 1,50,000 + 5,75,000 – 1,00,000)	3,60,000
Share of DEF Ltd.	16,25,000
	32,85,000

© The Institute of Chartered Accountants of India

3. Post-acquisition profits of XYZ Ltd. ₹

Profit after 1.10. 20X1 [8,20,000-1,00,000]x 6/12	3,60,000
Less: 10% depreciation on ₹ 20,00,000 for 6 months less depreciation already charged for 2nd half of 20X1-20X2 on ₹ 15,00,000 (1,00,000-75,000)	(25,000)
Share of DEF Ltd.	3,35,000

4. Consolidated total comprehensive income ₹

DEF Ltd.	
Retained earnings on 31.3.20X2	5,72,000
Less: Retained earnings as on 1.4.20X1	(0)
Profits for the year 20X1-20X2	5,72,000
Less: Elimination of intra-group dividend	(2,00,000)
Adjusted profit for the year	3,72,000
XYZ Ltd.	
Adjusted profit attributable to DEF Ltd. (W.N.3)	3,35,000
Consolidated profit or loss for the year	7,07,000

5. No Non-controlling Interest as 100% shares of XYZ Ltd. are held by DEF Ltd.

6. Gain on Bargain Purchase ₹

Amount paid for 20,000 shares		34,00,000
Par value of shares	20,00,000	
DEF Ltd.'s share in acquisition date profits of XYZ Ltd.	32,85,000	(52,85,000)
Gain on Bargain Purchase		18,85,000

7. Value of Plant & Machinery ₹

DEF Ltd.		24,00,000
XYZ Ltd.	13,50,000	
Add: Appreciation on 1.10. 20X1	5,75,000	
	19,25,000	
Add: Depreciation for 2nd half charged on pre-revalued value	75,000	
Less: Depreciation on ₹ 20,00,000 for 6 months	(1,00,000)	19,00,000
		43,00,000

© The Institute of Chartered Accountants of India

8. **Consolidated retained earnings** ₹

	DEF Ltd.	XYZ Ltd.	Total
As given	5,72,000	8,20,000	13,92,000
Consolidation Adjustments:			
(i) Elimination of pre-acquisition element [3,00,000 + 3,60,000]	0	(6,60,000)	(6,60,000)
(ii) Elimination of intra-group dividend	(2,00,000)	2,00,000	0
(iii) Impact of fair value adjustments	0	(25,000)	(25,000)
Adjusted retained earnings consolidated	3,72,000	3,35,000	7,07,000

Assumptions:

1. Investment in XYZ Ltd is carried at cost in the separate financial statements of DEF Ltd.
2. Appreciation of ₹10 lakhs in land & buildings is entirely attributable to land element only.
3. Depreciation on plant and machinery is on WDV method.
4. Acquisition-date fair value adjustment to inventories of XYZ Ltd. existing at the balance sheet date does not result in need for any write-down.

5. **Consolidated Balance Sheet of Ram Ltd. and its subsidiary, Krishan Ltd.**

as at 31st March, 20X2

Particulars	Note No.	₹
I. Assets		
(1) Non-current assets		
(i) Property, Plant & Equipment	1	17,20,000
(ii) Goodwill	2	1,65,800
(2) Current Assets		
(i) Inventories	3	3,42,800
(ii) Financial Assets		
(a) Trade Receivables	4	1,99,600
(b) Cash & Cash equivalents	5	45,000
Total Assets		**24,73,200**

© The Institute of Chartered Accountants of India

II. Equity and Liabilities		
(1) Equity	6	10,00,000
(i) Equity Share Capital	7	7,30,600
(ii) Other Equity		4,33,600
(2) Non-controlling Interest (WN 4)		
(3) Current Liabilities		
(i) Financial Liabilities	8	1,49,000
(a) Trade Payables	9	1,60,000
(b) Short term borrowings		**24,73,200**
Total Equity & Liabilities		

Notes to accounts

			₹
1.	**Property Plant & Equipment**		
	Land & Building	8,60,000	
	Plant & Machinery	8,60,000	17,20,000
2.	Goodwill		1,65,800
3.	**Inventories**		
	Ram Ltd.	2,40,000	
	Krishan Ltd.	1,02,800	3,42,800
4.	**Trade Receivables**		
	Ram Ltd.	1,19,600	
	Krishan Ltd.	80,000	1,99,600
5.	**Cash & Cash equivalents**		
	Ram Ltd.	29,000	
	Krishan Ltd.	16,000	45,000
8.	**Trade Payables**		
	Ram Ltd.	94,200	
	Krishan Ltd.	54,800	1,49,000
9.	**Short-term borrowings**		
	Bank overdraft		1,60,000

© The Institute of Chartered Accountants of India

Statement of Changes in Equity:

6. Equity share Capital

Balance at the beginning of the reporting period	Changes in Equity share capital during the year	Balance at the end of the reporting period
10,00,000	0	10,00,000

7. Other Equity

	Share application money	Equity component	Reserves & Surplus			Total
			Capital reserve	Retained Earnings	Other Reserves	
Balance at the beginning of the reporting period				0	6,00,000	6,00,000
Total comprehensive income for the year			0	1,14,400		1,14,400
Dividends			0	(24,000)		(24,000)
Total comprehensive income attributable to parent			0	40,200		40,200
Gain on Bargain purchase				0		0
Balance at the end of reporting period				1,30,600	6,00,000	7,30,600

Working Notes:

1. Adjustments of Fair Value

The Plant & Machinery of Krishan Ltd. would stand in the books at ₹ 2,85,000 on 1st October, 20X1, considering only six months' depreciation on ₹ 3,00,000 total depreciation being ₹ 30,000. The value put on the assets being ₹ 4,00,000 there is an appreciation to the extent of ₹ 1,15,000.

© The Institute of Chartered Accountants of India

2. Acquisition date profits of Krishan Ltd.

Reserves on 1.4. 20X1		2,00,000
Profit & Loss Account Balance on 1.4. 20X1		60,000
Profit for 20X1-20X2: Total (₹ 1,64,000 less ₹ 20,000) x 6/12 i.e. ₹ 72,000; upto 1.10. 20X1		72,000
Total Appreciation		3,25,000
		6,57,000
Holding Co. Share (60%)		3,94,200

3. Post-acquisition profits of Krishan Ltd.

Profit after 1.10. 20X1 [1,64,000-20,000]x 6/12	72,000
Less: 10% depreciation on ₹ 4,00,000 for 6 months less depreciation already charged for 2nd half of 20X1-20X2 on ₹ 3,00,000 (20,000-15,000)	(5,000)
Total	67,000
Share of holding Co. (60%)	40,200

4. Non-controlling Interest

Par value of 1600 shares	160,000
Add: 2/5 Acquisition date profits (6,57,000 – 40,000)	2,46,800
Add: 2/5 Post-acquisition profits [WN 3]	26,800
	4,33,600

5. Goodwill:

Amount paid for 2,400 shares		8,00,000
Par value of shares	2,40,000	
Acquisition date profits share of Ram Ltd.	3,94,200	(6,34,200)
Goodwill		1,65,800

© The Institute of Chartered Accountants of India

6. Value of Plant & Machinery:

Ram Ltd.		4,80,000
Krishan Ltd.	2,70,000	
Add: appreciation on 1.10. 20X1	1,15,000	
	3,85,000	
Add: Depreciation for 2nd half charged on pre-revalued value	15,000	
Less: Depreciation on ₹ 4,00,000 for 6 months	(20,000)	3,80,000
		8,60,000

7. Profit & Loss account consolidated

Ram Ltd. (as given)	1,14,400	
Less: Dividend	(24,000)	90,400
Share of Ram Ltd. in post-acquisition profits		40,200
		1,30,600

6. Blue Heavens Ltd. consolidated balance sheet at 31 March 20X2 will be calculated as follows: **(in lakhs)**

	Blue Heavens Ltd.	Orange County Ltd.	Consolidation adjustments	Consolidated Blue Heavens Ltd.
	Carrying amount	Carrying amount		
Assets				
Non-current assets				
Goodwill			1,300 (WN 1)	1,300
Buildings and other PPE	7,000	3,000	300	10,300
Financial Assets				
Investment in Orange County Ltd.	6,000		(6,000)	
Current assets				
Inventories	700	500	100	1,300
Financial Assets				
Trade receivables	300	250		550
Cash	1,500	700		2,200
Total assets	**15,500**	**4,450**		**15,650**

© The Institute of Chartered Accountants of India

Equity and liabilities				
Equity				
Share capital	5,000	2,000	(2,000)	5,000
Other Equity	10,200	2,300	(2,300)	10,200
Trade payable	300	150		450
Total liabilities and equity	**15,500**	**4,450**		**15,650**

Consolidation involves:

- Adding the balance sheet of the parent and its subsidiary together line by line.
- Eliminating the carrying amount of the parent's investment in the subsidiary (because it is replaced by the goodwill and the fair value of the assets, liabilities and contingent liabilities acquired) and the pre-acquisition equity of the subsidiary (because that equity was not earned or contributed by the group but is part of what was purchased) and recognising the fair value adjustments together with the goodwill asset that arose on acquisition of the subsidiary.

1. Working for goodwill:	(₹ in lakhs)
Consideration paid	6,000
Less: Acquisition date fair value of Orange County Ltd. net assets	(4,700)
Goodwill	1,300

2. Working for the acquisition date fair value of Orange County Ltd. net assets: Acquisition date fair value of acquiree (Orange County Ltd.) assets

Buildings and other PPE	3,300
Inventories	600
Trade receivables	250
Cash	700
Less: fair value of trade payables	(150)
Fair value of net assets acquired	4,700

7. Non-controlling interest

= 25 % × Orange County Ltd. identifiable net assets at fair value of ₹ 4,700

= ₹ 1,175.

© The Institute of Chartered Accountants of India

Blue Heavens Ltd.'s consolidated balance sheet at 31 March 20X2 will be calculated as follows: **(in lakhs)**

	Blue Heavens Ltd.	Orange County Ltd.	Consolidation adjustments	Consolidated Blue Heavens Ltd.
	Carrying amount	Carrying amount		
Assets				
Non-current assets				
Goodwill			975 (WN 1)	975
Buildings and other PPE	7,000	3,000	300	10,300
Financial Assets				
Investment in Orange County Ltd.	4,500		(4,500)	
Current assets				
Inventories	700	500	100	1,300
Financial Assets				
Trade receivables	300	250		550
Cash	3,000	700		3,700
Total assets	**15,500**	**4,450**		**16,825**
Equity and liabilities				
Equity				
Share capital	5,000	2,000	(2,000)	5,000
Other Equity	10,200	2,300	(2,300)	10,200
Non-controlling interest			1,175	1,175
Current liabilities				
Financial Liabilities				
Trade payables	300	150		450
Total liabilities and equity	**15,500**	**4,450**		**16,825**

Note: In this question, Blue Heavens Ltd.'s (and consequently the group's) cash balance is ₹ 1,500 lakh higher than in Question above because, here Blue Heavens Ltd. paid ₹ 1,500 less to acquire Orange County Ltd. (i.e. ₹ 6,000 less ₹ 4,500).

© The Institute of Chartered Accountants of India

1. **Working for goodwill:** (₹ in lakhs)

Consideration paid	4,500
Non- controlling interest	1,175
Less: Acquisition date fair value of Orange County Ltd. net assets	
(cal. as above)	4,700
Goodwill	975

(Goodwill recognized in the consolidated balance sheet relates solely to the acquirer's proportion of the subsidiary; it does not include the non-controlling interest's share).

8. Alternative I for calculation of Non-controlling Interest:

The Non-controlling Interest proportion of Orange County Ltd. is 25%.

At 31 March 20X3, the NCI in the consolidated balance sheet would be calculated as:

	₹ (lakh)
NCI at date of acquisition (31 March 20X2) (see solution to Question 7)	1,175
NCI's share of profit for the year ended 31 March 20X3, being 25% Of ₹ 435 lakh (being ₹ 550 profit of Orange County Ltd. as per Orange County Ltd. financial statements less ₹ 100 group inventory Fair value adjustment less ₹ 15 group depreciation on building fair value adjustment)*	109
NCI as at 31 March 20X3	1,284

*In calculating the NCI's share of profit for the year ended 31 March 20X3, no deduction is made for goodwill amortization because, as explained above, the goodwill arising on consolidation relates solely to the acquirer's proportion of the subsidiary and does not include the non-controlling interest's share.

Alternative II for calculation of Non-controlling Interest:

As an alternative to the above three-step approach, at 31 March 20X3 the NCI in the consolidated balance sheet is calculated as 25% (the NCI's proportion) of ₹ 5,135, which is ₹ 1,284. ₹ 5,135 is Orange County Ltd. net assets at 31 March 20X3 as shown in Orange County Ltd. balance sheet (₹ 4,850, being ₹ 5,020 assets less ₹ 170 liabilities) plus the fair value adjustment to those assets as made in preparing the group balance sheet (₹ 285, being the fair value adjustment in respect of Orange County Ltd. building, ₹ 300, less one year's depreciation of that adjustment, ₹ 15).

© The Institute of Chartered Accountants of India

Blue Heavens Ltd. consolidated statement of comprehensive income for the year ended 31 March 20X3 will be computed as follows:

	Blue Heavens Ltd.	Orange County Ltd.	Consolidate adjustments	Consolidated
Revenue	3,000	1,900		4,900
Cost of sales	(1,800)	(1,000)	(100) (WN 1)	(2,900)
Profit for the year	1,200	900		2,000
Administrative expenses	(400)	(350)	(113) (WN 2)	(863)
Total comprehensive income for the year	800	550		1,137

Total comprehensive income attributable to:

Owners of the parent (75%)	1,028
Non-controlling interest (25%)	109
	1,137

Consolidation involves:

- Adding the statement of comprehensive income of the parent and its subsidiary together line by line
- Recognising the fair value adjustments and/ or amortisation thereof together with amortisation of the goodwill asset that arose on acquisition of the subsidiary.

Blue Heavens Ltd. consolidated balance sheet at 31 March 20X3 will be computed as follows: **(₹ in lakh)**

	Blue Heavens Ltd.	Orange County Ltd.	Consolidation adjustments	Consolidated Blue Heavens Ltd.
	Carrying amount	Carrying amount		
Assets				
Non-current assets Goodwill			975-98 (WN 3)	877

© The Institute of Chartered Accountants of India

Buildings and other PPE	6,500	2,750	285 (WN 4)	9,535
Financial Assets				
Investment in Entity B	4,500		(4,500)	
Current assets				
Inventories	800	550		1,350
Financial Assets				
Trade receivables	380	300		680
Cash	4,170	1420		5,590
Total assets	**16,350**	**5,020**		**18,032**
Equity and liabilities Equity				
Share capital	5,000	2,000	(2,000)	5,000
Other Equity	11,000	2,850	(2,622) (WN 5)	11,228
Non-controlling interest			1,284	1,284
Current liabilities Financial Liabilities				
Trade payables	350	170		520
Total liabilities and equity	**16,350**	**5,020**		**18,032**

Consolidation involves:

- Adding the balance sheet of the parent and its subsidiary together line by line.
- Eliminating the carrying amount of the parent's investment in the subsidiary (because it is replaced by the goodwill and the fair value of the assets, liabilities and contingent liabilities acquired) and the pre-acquisition equity of the subsidiary (because that equity was not earned or contributed by the group but is part of what was purchased), and recognising the fair value adjustments together with the goodwill asset that arose on acquisition of the subsidiary as adjusted to reflect the first year post-acquisition
- Recognising the non-controlling interest in the net assets of Entity B.

Working Notes:

(1) Cost of sales adjustment:

₹ 100 = fair value adjustment in respect of inventories at 31 March 20X2.

© The Institute of Chartered Accountants of India

(2) Administrative expenses adjustment:

₹ 113 = Impairment of goodwill ₹ 98 (WN 3) + additional depreciation on building ₹ 15 (WN 4).

For simplicity it is assumed that all the goodwill impairment and the additional depreciation on buildings (on account of fair value adjustment) is adjusted against administrative expenses.

(3) Working for goodwill:

Goodwill at the acquisition date, ₹ 975, less accumulated impairment, ₹ 98 = ₹ 877.

(4) Working for building consolidation adjustment:

The fair value adjustment at 31 March 20X2 in respect of Orange County Ltd. building was ₹ 300, that is, the carrying amount at 31 March 20X2 was ₹ 300 lower than was recognized in the group's consolidated balance sheet. The building is being depreciated over 20 years from 31 March 20X2. Thus, at 31 March 20X3 the adjustment required on consolidation to the balance sheet will be ₹ 285, being ₹ 300 × 19/20 years' estimated useful life remaining. The additional depreciation recognized in the consolidated statement of comprehensive income is ₹ 15 (being ₹ 300 x 1/20).

(5) Reserves adjustment:

₹ 2,300 adjustment at the acquisition date (Question 7)

plus ₹ 98 (WN 3) impairment of goodwill

plus ₹ 15 (WN 4) additional depreciation on building

plus ₹ 100 (WN 1) fair value adjustment in respect of inventories

plus ₹ 109 NCI's share of Orange County Ltd. profit for the year (as included in the consolidated statement of comprehensive income)

= ₹ 2,622.

8. When 100% shares sold to independent party Consolidated Balance Sheet of P Pvt. Ltd. and its remaining subsidiaries as at 31st March, 20X2

Particulars	Note No.	(₹ in millions)
I. Assets		
(1) Non-current assets		
(i) Property Plant & Equipment	1	1,900
(ii) Goodwill	2	200
(2) Current Assets		
(i) Inventories	3	100

© The Institute of Chartered Accountants of India

(ii) Financial Assets		
(a) Trade Receivables	4	800
(b) Cash & Cash equivalents	5	5,100
Total Assets		**8,100**
II. **Equity and Liabilities**		
(1) Equity		
(i) Equity Share Capital	6	1,600
(ii) Other Equity	7	4,700
(2) Non-controlling Interest		
(3) Current Liabilities		
(i) Financial Liabilities		
(a) Trade Payables	8	1,800
Total Equity & Liabilities		**8,100**

Notes to accounts:

			(₹ in millions)
1.	**Property Plant & Equipment**		
	Land & Building	3,240	
	Less: S Pvt. Ltd.	(1,340)	1,900
2.	**Goodwill**	380	
	Less: S Pvt. Ltd.	(180)	200
3.	**Inventories**		
	Group	140	
	Less: S Pvt. Ltd.	(40)	100
4.	**Trade Receivables**		
	Group	1,700	
	Less: S Pvt. Ltd.	(900)	800
5.	**Cash & Cash equivalents**		
	Group (WN 2)	5,100	5,100
6.	**Trade Payables**		
	Group	2,700	
	Less: S Pvt. Ltd.	900	1,800

© The Institute of Chartered Accountants of India

Statement of changes in Equity:

6. Equity share Capital

Balance at the beginning of the reporting period	Changes in Equity share capital during the year	Balance at the end of the reporting period
1600	0	1600

7. Other Equity

	Share application money	Equity component	Reserves & Surplus			Total
			Capital reserve	Retained Earnings	Securities Premium	
Balance at the beginning				4,260		4,260
Total comprehensive income for the year			0			
Dividends			0			
Total comprehensive income attributable to parent			0			
Gain on disposal of S Pvt. Ltd.				440		440
Balance at the end of reporting period			0	4,700		4,700

Working Notes:

1. When sold, the carrying amount of all assets and liabilities attributable to S Pvt. Ltd. were eliminated from the consolidated balance sheet.

2. Cash on hand (in millions):

Cash before disposal of S Pvt. Ltd.	3,100
Less: S Pvt. Ltd. Cash	(1,000)
Add: Cash realized from disposal	3,000
Cash on Hand	5,100

3. Gain/ Loss on disposal of entity (in millions):

Proceeds from disposal	3,000
Less: Net assets of S Pvt. Ltd.	(2,560)
Gain on disposal	440

© The Institute of Chartered Accountants of India

4. Retained Earnings (in millions):

Retained Earnings before disposal	4,260
Add: Gain on disposal	440
Retained earnings after disposal	4,700

10. When 90% shares sold to independent party Consolidated Balance Sheet of Reliance Ltd. and its remaining subsidiaries as at 31st March, 20X2

Particulars	**Note No.**	**(₹ In '000)**
I. Assets		
(1) Non-current assets		
(i) Property Plant & Equipment	1	950
(ii) Goodwill	2	100
(iii) Financial Assets		
(a) Investments	3	128
(2) Current Assets		
(i) Inventories	4	50
(ii) Financial Assets		
(b) Trade Receivables	5	400
(c) Cash & Cash equivalents	6	2,050
Total Assets		**3,678**
II. Equity and Liabilities		
(1) Equity		
(i) Equity Share Capital	7	800
(ii) Other Equity	8	1,978
(2) Current Liabilities		
(i) Financial Liabilities		
(a) Trade Payables	9	900
Total Equity & Liabilities		**3,678**

Notes to accounts:

			(₹ In '000)
1.	**Property Plant & Equipment**		
	Land & Building	1620	
	Less: Reliance Jio Infocomm Ltd.	(670)	950

© The Institute of Chartered Accountants of India

2.	Goodwill	190	
	Less: Reliance Jio Infocomm Ltd.	(90)	100
3.	**Investments**		
	Investment in Reliance Jio Infocomm Ltd. (WN 2)	128	128
4.	**Inventories**		
	Group	70	
	Less: Reliance Jio Infocomm Ltd.	(20)	50
5.	**Trade Receivables**		
	Group	850	
	Less: Reliance Jio Infocomm Ltd.	(450)	400
6.	**Cash & Cash equivalents**		
	Group (WN 3)	2,050	2,050
9.	**Trade Payables**		
	Group	1,350	
	Less: Reliance Jio Infocomm Ltd.	450	900

Statement of changes in Equity:

7. Equity share Capital

Balance at the beginning of the reporting period	Changes in Equity share capital during the year	Balance at the end of the reporting period
800	0	800

8. Other Equity

	Share application money	Equity component	Reserves & Surplus			Total
			Capital reserve	Retained Earnings	Securities Premium	
Balance at the beginning				2,130		2,130
Total comprehensive income for the year			0			
Dividends			0			
Total			0			

© The Institute of Chartered Accountants of India

comprehensive Income attributable to parent						
Loss on disposal of Reliance Jio Infocomm Ltd.				(152)		(152)
Balance at the end of reporting period			0	1,978		1,978

Working Notes:

1. When 90% being sold, the carrying amount of all assets and liabilities attributable to Reliance Jio Infocomm Ltd. were eliminated from the consolidated balance sheet and further financial asset is recognized for remaining 10%.

2. Carrying value of remaining investment (in '000):

Net Assets of Reliance Ltd.	1,280
Less: 90% disposal	(1152)
Financial Asset	128

3. Cash on hand (in '000):

Cash before disposal of Reliance Jio Infocomm Ltd.	1,550
Less: Reliance Jio Infocomm Ltd. Cash	(500)
Add: Cash realized from disposal	1,000
Cash on Hand	2,050

4. Gain/ Loss on disposal of entity (in '000):

Proceeds from disposal	1,000
Less: Proportionate (90%) Net assets of Reliance Jio Infocomm Ltd. (90% of 1,280)	(1,152)
Loss on disposal	(152)

5. Retained Earnings (in '000):

Retained Earnings before disposal	2,130
Less: Loss on disposal	(152)
Retained earnings after disposal	1,978

© The Institute of Chartered Accountants of India

11. Journal Entries in Airtel Infrastructures Pvt. Ltd.

1.	Assets (Building) A/c	Dr.	10,25,000	
	To Cash			10,25,000
2.	Depreciation (P/L) A/c	Dr.	25,000	
	To Asset (Building)			25,000
3.	Cash A/c	Dr.	11,00,000	
	To Asset (Building)			10,00,000
	To Gain on sale of asset (P/L)			1,00,000

Journal Entries in Airtel Telecommunications Ltd.

1.	Asset (Building) A/c	Dr.	11,00,000	
	To Cash			11,00,000
2.	Depreciation (P/L) A/c	Dr.	37,500	
	To Assets (Building)			37,500

Journal entry for consolidation:

1.	Gain on sale of asset (P/L)	Dr.	1,00,000	
	To Asset (Building) A/c			1,00,000
2.	Asset (Building) A/c	Dr.	5,000 (WN 1)	
	To Consolidated P&L			5,000

Working Note:

To be depreciated on original value	(10,00,000-3,50,000)/20	32,500
Depreciation charged	(11,00,000-3,50,000)/20	37,500
Reversal of depreciation		**5,000**

Particulars	Consolidated financial statements	Individual Financial statements	
		Airtel Telecommunications Ltd.	Airtel Infrastructures Pvt. Ltd.
31st March 20X1	10,00,000	0	10,00,000
1st April 20X1 purchase sale	0	11,00,000	(10,00,000)
Depreciation	(32,500)	(37,500)	0
31st March 20X2	9,67,500	10,62,500	0

© The Institute of Chartered Accountants of India

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

(a) derecognises the assets and liabilities of the former subsidiary from the consolidated balance sheet.

(b) recognises any investment retained in the former subsidiary at its fair value when control is lost and subsequently accounts for it and for any amounts owed by or to the former subsidiary in accordance with relevant Ind ASs. That fair value shall be regarded as the fair value on initial recognition of a financial asset in accordance with Ind AS 109 or, when appropriate, the cost on initial recognition of an investment in an associate or joint venture.

(c) recognises the gain or loss associated with the loss of control attributable to the former controlling interest."

Paragraph B98(c) of Ind AS 110 states that on loss of control over a subsidiary, a parent shall reclassify to profit or loss, or transfer directly to retained earnings if required by other Ind AS, the amounts recognized in other comprehensive income in relation to the subsidiary on the basis specified in paragraph B99.

As per paragraph B99, if a parent loses control of a subsidiary, the parent shall account for all amounts previously recognized in other comprehensive income in relation to that subsidiary on the same basis as would be required if the parent had directly disposed of the related assets or liabilities.

Therefore, if a gain or loss previously recognized in other comprehensive income would be reclassified to profit or loss on the disposal of the related assets or liabilities, the parent shall reclassify the gain or loss from equity to profit or loss (as a reclassification adjustment) when it loses control of the subsidiary. If a revaluation surplus previously recognized in other comprehensive income would be transferred directly to retained earnings on the disposal of the asset, the parent shall transfer the revaluation surplus directly to retained earnings when it loses control of the subsidiary.

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

(a) re-classify the FVOCI reserve in respect of the debt investments of ₹ 5.4 crore (90% of ₹ 6 crore) attributable to the owners of the parent to the statement of profit or loss in accordance with paragraph B5.7.1A of Ind AS 109, Financial Instruments which requires that the cumulative gains or losses previously recognised in OCI shall be recycled to profit and loss upon derecognition of the related financial asset. This is reflected in the gain on disposal. Remaining 10% (i.e., ₹ 0.6 crore) relating to non-controlling interest (NCI) is included as part of the carrying amount of the non-controlling interest that is derecognised in calculating the gain or loss on loss of control of the subsidiary;

(b) transfer the reserve relating to the net measurement losses on the defined benefit liability of ₹ 2.7 crore (90% of ₹ 3 crore) attributable to the owners of the parent within

© The Institute of Chartered Accountants of India

equity to retained earnings. It is not reclassified to profit or loss. The remaining 10% (i.e., ₹ 0.3 crore) attributable to the NCI is included as part of the carrying amount of NCI that is derecognised in calculating the gain or loss on loss of control over the subsidiary. No amount is reclassified to profit or loss, nor is it transferred within equity, in respect of the 10% attributable to the non-controlling interest.

(c) reclassify the cumulative gain on fair valuation of equity investment of ₹ 3.6 crore (90% of ₹ 4 crore) attributable to the owners of the parent from OCI to retained earnings under equity as per paragraph B5.7.1 of Ind AS 109, Financial Instruments, which provides that in case an entity has made an irrevocable election to recognise the changes in the fair value of an investment in an equity instrument not held for trading in OCI, it may subsequently transfer the cumulative amount of gains or loss within equity. Remaining 10% (i.e., ₹ 0.4 crore) related to the NCI are derecognised along with the balance of NCI and not reclassified to profit and loss.

(d) reclassify the foreign currency translation reserve of ₹ 7.2 crore (90% × ₹ 8 crore) attributable to the owners of the parent to statement of profit or loss as per paragraph 48 of Ind AS 21, The Effects of Changes in Foreign Exchange Rates, which specifies that the cumulative amount of exchange differences relating to the foreign operation, recognised in OCI, shall be reclassified from equity to profit or loss on the disposal of foreign operation. This is reflected in the gain on disposal. Remaining 10% (i.e., ₹ 0.8 crore) relating to the NCI is included as part of the carrying amount of the NCI that is derecognised in calculating the gain or loss on the loss of control of subsidiary, but is not reclassified to profit or loss in pursuance of paragraph 48B of Ind AS 21, which provides that the cumulative exchange differences relating to that foreign operation attributed to NCI shall be derecognised on disposal of the foreign operation, but shall not be reclassified to profit or loss.

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

(₹ in crore)

Particular		Amount (Dr)	Amount (Cr)	PL Impact	RE Impact
Gain/Loss on Disposal on Investments					
Bank	Dr.	56			
Non-controlling interest (Derecognised)	Dr.	6			
Investment at FV (20% Retained)	Dr.	16			
To Gain on Disposal (PL) - ***balancing figure***			18	18	
To De-recognition of total net assets of subsidiary			60		

© The Institute of Chartered Accountants of India

Reclassification of FVTOCI reserve on debt instruments to profit or loss				
FVTOCI reserve on debt instruments Dr. (6 cr. x 90%)	5.4			
To Profit and loss		5.4	5.4	
Reclassification of net measurement loss reserve to profit or loss				
Retained Earnings Dr.	2.7			-2.7
To Net measurement loss reserve (FVTOCI) [(3 cr. x 90%)]		2.7		
Reclassification of FVTOCI reserve on equity instruments to retained earnings				
FVTOCI reserve on equity instruments (4 cr.x 90%) Dr.	3.6			
To Retained earnings		3.6		3.6
Foreign currency translation reserve reclassified to profit or loss				
Foreign currency translation reserve (FVOCI) [8 cr. x 90%] Dr.	7.2			
To Profit and loss		7.2	7.2	
Total			30.6	0.9

13. Calculation of Investor Ltd.'s investment in XYZ Ltd. under equity method:

	₹	₹
Acquisition of investment in XYZ Ltd.		
Share in book value of XYZ Ltd.'s net assets (35% of ₹ 90,00,000)	31,50,000	
Share in fair valuation of XYZ Ltd.'s net assets [35% of (₹ 1,10,00,000 – ₹ 90,00,000)]	7,00,000	
Goodwill on investment in XYZ Ltd. (balancing figure)	9,00,000	
Cost of investment		**47,50,000**
Profit during the year		
Share in the profit reported by XYZ Ltd. (35% of ₹ 8,00,000)	2,80,000	

© The Institute of Chartered Accountants of India

Adjustment to reflect effect of fair valuation [35% of (₹ 20,00,000/10 years)]	(70,000)	
Share of profit in XYZ Ltd. recognised in income by Investor Ltd.		**2,10,000**
Long term equity investment		
FVTOCI gain recognised in OCI (35% of ₹ 2,00,000)		70,000
Dividend received by Investor Ltd. during the year [35% of ₹ 12,00,000]		(4,20,000)
Closing balance of Investor Ltd.'s investment in XYZ Ltd.		**46,10,000**

14. As provided in Ind- AS 111 - Joint Arrangements - this is a joint arrangement because two or more parties have joint control of the property under a contractual arrangement. The arrangement will be regarded as a joint operation because Alpha Ltd. and Gama Ltd. have rights to the assets and obligations for the liabilities of this joint arrangement. This means that the company and the other investor will each recognise 50% of the cost of constructing the asset in property, plant and equipment.

The borrowing cost incurred on constructing the property should under the principles of Ind AS 23 'Borrowing Costs', be included as part of the cost of the asset for the period of construction.

In this case, the relevant borrowing cost to be included is ₹ 50,00,000 (₹ 10,00,00,000 x 10% x 6/12).

The total cost of the asset is ₹ 40,50,00,000 (₹ 40,00,00,000 + ₹ 50,00,000) ₹ 20,25,00,000 crores is included in the property, plant and equipment of Alpha Ltd. and the same amount in the property, plant and equipment of Gama Ltd.

The depreciation charge for the year ended 31 March 20X2 will therefore be ₹ 1,01,25,000 (₹ 40,50,00,000 x 1/20 x 6/12) ₹ 50,62,500 will be charged in the statement of profit or loss of the company and the same amount in the statement of profit or loss of Gama Ltd.

The other costs relating to the arrangement in the current year totalling ₹ 54,00,000 (finance cost for the second half year of ₹ 50,00,000 plus maintenance costs of ₹ 4,00,000) will be charged to the statement of profit or loss of Alpha Ltd. and Gama Ltd. in equal proportions- ₹ 27,00,000 each.

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

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

© The Institute of Chartered Accountants of India

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

(ii) its debt or equity instruments are not traded in a public market (a domestic or foreign stock exchange or an over-the-counter market, including local and regional markets);

(iii) it did not file, nor is it in the process of filing, its financial statements with a securities commission or other regulatory organisation for the purpose of issuing any class of instruments in a public market; and

(iv) its ultimate or any intermediate parent produces financial statements that are available for public use and comply with Ind ASs, in which subsidiaries are consolidated or are measured at fair value through profit or loss in accordance with this Ind AS.

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

— wholly-owned subsidiary; or

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

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

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

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

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

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

© The Institute of Chartered Accountants of India

FOR SHORTCUT TO IND AS WISDOM: SCAN ME!

TEST YOUR KNOWLEDGE

Questions

1. Company A intends to restate its past business combinations with effect from 30 June 20X0 (being a date prior to the transition date).

   If business combinations are restated, whether certain other exemptions, such as the deemed cost exemption for property, plant and equipment (PPE), can be adopted?

2. X Ltd. was using cost model for its property, plant and equipment till March 31, 20X2 under previous GAAP. The Ind AS become applicable to the company for financial year beginning April 1, 20X2. On April 1, 20X1, i.e., the date of its transition to Ind AS, it used fair value as the deemed cost in respect of its property, plant and equipment. X Ltd. wants to follow revaluation model as its accounting policy in respect of its property, plant and equipment for the first annual Ind AS financial statements.

   Whether use of fair values as deemed cost on the date of transition and use of revaluation model in the first annual Ind AS financial statements would amount to a change in accounting policy?

3. Y Ltd. is a first time adopter of Ind AS. The date of transition is April 1, 20X5. On April 1, 20X0, it obtained a 7 year US $ 1,00,000 loan. It has been exercising the option provided in Paragraph 46/46A of AS 11 and has been amortising the exchange differences in respect of this loan over the balance period of such loan. On the date of transition to Ind AS, Y Ltd. wants to discontinue the accounting policy as per the previous GAAP and follow the requirements of Ind AS 21 with respect to recognition of foreign exchange differences.

   Whether the Company is permitted to do so?

4. A company has chosen to elect the deemed cost exemption in accordance with Ind AS 101. However, it does not wish to continue with its existing policy of capitalising exchange

© The Institute of Chartered Accountants of India

fluctuation on long term foreign currency monetary items to property, plant and equipment i.e. it does not want to elect the exemption available as per Ind AS 101.

In such a case, how would the company be required to adjust the foreign exchange fluctuation already capitalised to the cost of property, plant and equipment under previous GAAP?

5. XYZ Pvt. Ltd. is a company registered under the Companies Act, 2013 following Accounting Standards notified under Companies (Accounting Standards) Rules, 2006. The Company has decided to voluntarily adopt Ind AS w.e.f 1st April, 20X2 with a transition date of 1st April, 20X1.

The Company has one Wholly Owned Subsidiary and one Joint Venture which are into manufacturing of automobile spare parts.

The consolidated financial statements of the Company under Indian GAAP are as under:

Consolidated Financial Statements

(₹ in Lakhs)

Particulars	31.03.20X2	31.03.20X1
Shareholder's Funds		
Share Capital	7,953	7,953
Reserves & Surplus	16,547	16,597
Non-Current Liabilities		
Long Term Borrowings	1,000	1,000
Long Term Provisions	1,101	691
Other Long-Term Liabilities	5,202	5,904
Current Liabilities		
Trade Payables	9,905	8,455
Short Term Provisions	500	475
Total	**42,208**	**41,075**
Non-Current Assets		
Property Plant & Equipment	21,488	22,288
Goodwill on Consolidation of subsidiary and JV	1,507	1,507
Investment Property	5,245	5,245
Long Term Loans & Advances	6,350	6,350
Current Assets		
Trade Receivables	4,801	1,818

© The Institute of Chartered Accountants of India

Investments ·	1,263	3,763
Other Current Assets	1,554	104
Total	**42,208**	**41,075**

Additional Information:

The Company has entered into a joint arrangement by acquiring 50% of the equity shares of ABC Pvt. Ltd. Presently, the same has been accounted as per the proportionate consolidated method. The proportionate share of assets and liabilities of ABC Pvt. Ltd. included in the consolidated financial statement of XYZ Pvt. Ltd. is as under:

Particulars	₹ in Lakhs
Property, Plant & Equipment	1,200
Long Term Loans & Advances	405
Trade Receivables	280
Other Current Assets	50
Trade Payables	75
Short Term Provisions	35

The Investment is in the nature of Joint Venture as per Ind AS 111.

Suggest the accounting adjustments which are required to be made in the opening Balance Sheet as on 1st April, 20X1.

6. Mathur India Private Limited has to present its first financials under Ind AS for the year ended 31st March, 20X3. The transition date is 1st April, 20X1.

The following adjustments were made upon transition to Ind AS:

(a) The Company opted to fair value its land as on the date on transition.

The fair value of the land as on 1st April, 20X1 was ₹ 10 crores. The carrying amount as on 1st April, 20X1 under the existing GAAP was ₹ 4.5 crores.

(b) The Company has recognised a provision for proposed dividend of ₹ 60 lacs and related dividend distribution tax of ₹ 18 lacs during the year ended 31st March, 20X1. It was written back as on opening balance sheet date.

(c) The Company fair values its investments in equity shares on the date of transition. The increase on account of fair valuation of shares is ₹ 75 lacs.

(d) The Company has an Equity Share Capital of ₹ 80 crores and Redeemable Preference Share Capital of ₹ 25 crores.

(e) The reserves and surplus as on 1st April, 20X1 before transition to Ind AS was ₹ 95 crores representing ₹ 40 crores of general reserve and ₹ 5 crores of capital

© The Institute of Chartered Accountants of India

reserve acquired out of business combination and balance is surplus in the Retained Earnings.

(f) The company identified that the preference shares were in nature of financial liabilities.

What is the balance of total equity (Equity and other equity) as on 1st April, 20X1 after transition to Ind AS? Show reconciliation between total equity as per AS (Accounting Standards) and as per Ind AS to be presented in the opening balance sheet as on 1st April, 20X1.

Ignore deferred tax impact.

7. ABC Ltd is a government company and is a first-time adopter of Ind AS. As per the previous GAAP, the contributions received by ABC Ltd. from the government (which holds 100% shareholding in ABC Ltd.) which is in the nature of promoters' contribution have been recognised in capital reserve and treated as part of shareholders' funds in accordance with the provisions of AS 12, Accounting for Government Grants.

   State whether the accounting treatment of the grants in the nature of promoters' contribution as per AS 12 is also permitted under Ind AS 20 Accounting for Government Grants and Disclosure of Government Assistance. If not, then what will be the accounting treatment of such grants recognised in capital reserve as per previous GAAP on the date of transition to Ind AS.

Answers

1. Ind-AS 101 prescribes that an entity may elect to use one or more of the exemptions of the Standard. As such, an entity may choose to adopt a combination of optional exemptions in relation to the underlying account balances.

When the past business combinations after a particular date (30 June 20X0 in the given case) are restated, it requires retrospective adjustments to the carrying amounts of acquiree's assets and liabilities on account of initial acquisition accounting of the acquiree's net assets, the effects of subsequent measurement of those net assets (including amortisation of non-current assets that were recognised at its fair value), goodwill on consolidation and the consolidation adjustments. Therefore, the goodwill and equity (including non-controlling interest (NCI)) cannot be computed by considering the deemed cost exemption for PPE. However, the entity may adopt the deemed cost exemption for its property, plant and equipment other than those acquired through business combinations.

2. In the instant case, X Ltd. is using revaluation model for property, plant and equipment for the first annual Ind AS financial statements and using fair value of property, plant and equipment on the date of the transition, as deemed cost. Since the entity is using fair value at the transition date as well as in the first Ind AS financial statements, there is no change in accounting policy and mere use of the term 'deemed cost' would not mean that there is a change in accounting policy.

© The Institute of Chartered Accountants of India

3. Ind AS 101 provides that a first-time adopter may continue the policy adopted for accounting for exchange differences arising from translation of long-term foreign currency monetary items recognised in the financial statements for the period ending immediately before the beginning of the first Ind AS financial reporting period as per the previous GAAP. Ind AS 101 gives an option to continue the existing accounting policy. Hence, Y Ltd. may opt for discontinuation of accounting policy as per previous GAAP and follow the requirements of Ind AS 21. The cumulative amount lying in the Foreign Currency Monetary Item Translation Difference Account (FCMITDA) as per AS 11 should be derecognised by an adjustment against retained earnings on the date of transition.

4. Ind AS 101 permits to continue with the carrying value for all of its property, plant and equipment as per the previous GAAP and use that as deemed cost for the purposes of first time adoption of Ind AS. Accordingly, the carrying value of property, plant and equipment as per previous GAAP as at the date of transition need not be adjusted for the exchange fluctuations capitalized to property, plant and equipment. Separately, it allows a company to continue with its existing policy for accounting for exchange differences arising from translation of long term foreign currency monetary items recognised in the financial statements for the period ending immediately before the beginning of the first Ind AS financial reporting period as per the previous GAAP. Accordingly, given that Ind AS 101 provides these two choices independent of each other, it may be possible for an entity to choose the deemed cost exemption for all of its property, plant and equipment and not elect the exemption of continuing the previous GAAP policy of capitalising exchange fluctuation to property, plant and equipment. In such a case, in the given case, a harmonious interpretation of the two exemptions would require the company to recognise the property, plant and equipment at the transition date at the previous GAAP carrying value (without any adjustment for the exchanges differences capitalized under previous GAAP) but for the purposes of the first (and all subsequent) Ind AS financial statements, foreign exchange fluctuation on all long term foreign currency borrowings that arose after the transition date would be recognised in the statement of profit and loss.

5. As per paras D31AA and D31AB of Ind AS 101, when changing from proportionate consolidation to the equity method, an entity shall recognise its investment in the joint venture at transition date to Ind AS.

   That initial investment shall be measured as the aggregate of the carrying amounts of the assets and liabilities that the entity had previously proportionately consolidated, including any goodwill arising from acquisition. If the goodwill previously belonged to a larger cash-generating unit, or to a group of cash-generating units, the entity shall allocate goodwill to the joint venture on the basis of the **relative** carrying amounts of the joint venture and the cash-generating unit or group of cash-generating units to which it belonged. The balance of the investment in joint venture at the date of transition to Ind AS, determined in accordance with paragraph D31AA above is regarded as the deemed cost of the investment at initial recognition.

© The Institute of Chartered Accountants of India

Accordingly, the deemed cost of the investment will be

Property, Plant & Equipment	1,200
Goodwill (Refer Note below)	119
Long Term Loans & Advances	405
Trade Receivables	280
Other Current Assets	50
Total Assets	2,054
Less: Trade Payables	75
Short Term Provisions	35
Deemed cost of the investment in JV	1,944

Calculation of proportionate goodwill share of Joint Venture ie ABC Pvt. Ltd.

Property, Plant & Equipment	22,288
Goodwill	1,507
Long Term Loans & Advances	6,350
Trade Receivables	1,818
Other Current Assets	104
Total Assets	32,067
Less: Trade Payables	8,455
Short Term Provisions	475
	23,137

Note: Only those assets and liabilities have been taken into account for calculation of 'proportionate goodwill share of Joint Venture', which were given in the question as 'proportionate share of assts and liabilities of ABC Ltd. added to XYZ Ltd.'

Proportionate Goodwill of Joint Venture

= [(Goodwill on consolidation of subsidiary and JV/Total relative net asset) x Net asset of JV]

= (1507 / 23,137) x 1825 = 119 (approx.)

Accordingly, the proportional share of assets and liabilities of Joint Venture will be removed from the respective values assets and liabilities appearing in the balance sheet on 31.3.20X1 and Investment in JV will appear under non-current asset in the transition date balance sheet as on 1.4.20X1.

Adjustments made in previous GAAP balance sheet to arrive at Transition date Ind AS Balance Sheet

© The Institute of Chartered Accountants of India

Transition Date Ind AS Balance Sheet of XYZ Pvt. Ltd. as at 1st April, 20X1

Particulars	Previous GAAP	Ind AS Adjustment	Ind AS GAAP
Non-Current Assets			
Property, Plant & Equipment	22,288	(1,200)	21,088
Investment Property	5,245	-	5,245
Intangible assets - Goodwill on Consolidation	1,507	(119)	1,388
Financial Assets			
Long Term Loans & Advances	6,350	(405)	5,945
Non- current investment in JV	-	1,944	1,944
Current Assets	-		
Financial Assets			
Investments ·	3,763	-	3,763
Trade Receivables	1,818	(280)	1,538
Other Current Assets	104	(50)	54
Total	**41,075**	**(110)**	**40,965**
Equity and liabilities			
Equity			
Share Capital	7,953	-	7,953
Other equity	16,597	-	16,597
Non-Current Liabilities			
Financial Liabilities			
Borrowings	1,000		1,000
Long Term Provisions	691		691
Other Long-Term Liabilities	5,904		5,904
Current Liabilities			
Financial Liabilities			
Trade Payables	8,455	(75)	8,380
Short Term Provisions	475	(35)	440
Total	**41,075**	**(110)**	**40,965**

© The Institute of Chartered Accountants of India

6. **Computation of balance total equity as on 1st April, 20X1 after transition to Ind AS**

			₹ in crore
Share capital- Equity share Capital			80
Other Equity			
General Reserve		40	
Capital Reserve		5	
Retained Earnings (95-5-40)	50		
Add: Increase in value of land (10-4.5)	5.5		
Add: De recognition of proposed dividend (0.6 + 0.18)	0.78		
Add: Increase in value of Investment	0.75	57.03	102.03
Balance total equity as on 1st April, 20X1 after transition to Ind AS			182.03

Reconciliation between Total Equity as per AS and Ind AS to be presented in the opening balance sheet as on 1st April, 20X1

		₹ in crore
Equity share capital		80
Redeemable Preference share capital		25
		105
Reserves and Surplus		95
Total Equity as per AS		200
Adjustment due to reclassification		
Preference share capital classified as financial liability		(25)
Adjustment due to derecognition		
Proposed Dividend not considered as liability as on 1st April 20X1		0.78
Adjustment due to remeasurement		
Increase in the value of Land due to remeasurement at fair value	5.5	
Increase in the value of investment due to remeasurement at fair value	0.75	6.25
Equity as on 1st April, 20X1 after transition to Ind AS		182.03

7. Paragraph 2 of Ind AS 20, "Accounting for Government Grants and Disclosure of Government Assistance" inter alia states that the Standard does not deal with government participation in the ownership of the entity.

Since ABC Ltd. is a Government company, it implies that government has 100% shareholding in the entity. Accordingly, the entity needs to determine whether the payment

is provided as a shareholder contribution or as a government. Equity contributions will be recorded in equity while grants will be shown in the Statement of Profit and Loss.

Where it is concluded that the contributions are in the nature of government grant, the entity shall apply the principles of Ind AS 20 retrospectively as specified in Ind AS 101 'First Time Adoption of Ind AS'. Ind AS 20 requires all grants to be recognised as income on a systematic basis over the periods in which the entity recognises as expenses the related costs for which the grants are intended to compensate. Unlike AS 12, Ind AS 20 requires the grant to be classified as either a capital or an income grant and does not permit recognition of government grants in the nature of promoter's contribution directly to shareholders' funds.

Where it is concluded that the contributions are in the nature of shareholder contributions and are recognised in capital reserve under previous GAAP, the provisions of paragraph 10 of Ind AS 101 would be applied which states that except in certain cases, an entity shall in its opening Ind AS Balance Sheet:

(a) recognise all assets and liabilities whose recognition is required by Ind AS;

(b) not recognise items as assets or liabilities if Ind AS do not permit such recognition;

(c) reclassify items that it recognised in accordance with previous GAAP as one type of asset, liability or component of equity, but are a different type of asset, liability or component of equity in accordance with Ind AS; and

(d) apply Ind AS in measuring all recognised assets and liabilities.

Accordingly, as per the above requirements of paragraph 10(c) in the given case, contributions recognised in the Capital Reserve should be transferred to appropriate category under 'Other Equity' at the date of transition to Ind AS.

© The Institute of Chartered Accountants of India

5. CASE STUDIES BASED ON IND AS

Case Study 1

On 1 April 20X1, Star Limited has advanced a housing loan of ₹ 15 lakhs to one of its employees at an interest rate of 6% per annum which is repayable in 5 equal annual installments along with interest at each year end. Employee is not required to give any specific performance against this benefit. The market rate of similar loan for housing finance by banks is 10% per annum.

The accountant of the company has recognized the staff loan in the balance sheet equivalent to the amount of housing loan disbursed i.e. ₹ 15 lakhs. The interest income for the year is recognized at the contracted rate in the Statement of Profit and Loss by the company i.e. ₹ 90,000 (6% of ₹ 15 lakhs).

Analyze whether the above accounting treatment made by the accountant is in compliance with the relevant Ind AS. If not, advise the correct treatment of housing loan, interest and other expenses in the financial statements of Star Limited for the year 20X1-20X2 along with workings and applicable Ind AS.

You are required to explain how the housing loan should be reflected in the Ind AS compliant Balance Sheet of Star Limited on 31 March 20X2.

Solution

The accounting treatment made by the accountant is not in compliance with Ind AS 109 'Financial Instruments'. As per Ind AS 109, at initial recognition, an entity shall measure a financial asset or financial liability at its fair value. The fair value of a financial instrument at initial recognition is normally the transaction price i.e. the fair value of the consideration given or received.

After initial recognition, an entity shall measure a financial asset either at amortised cost or at fair value through profit and loss or fair value through other comprehensive income.

Here, the loan given to employee is not at market rate. Hence, the fair value of the loan will not be equal to its initial loan proceeds. As per Ind AS 109, a financial instrument is initially measured and recorded in the books at its fair value. Further, interest income to be recognised in the Statement of Profit and Loss will be the finance income recognised at effective rate of interest i.e. @ 10% and not the rate of interest charged by the company i.e. @ 6%.

The correct accounting treatment as per Ind AS 109 will be as under:

For measuring the fair value or present value of the loan at initial recognition, market rate of interest of similar loan is considered (level 1 observable input) ie @ 10%, to discount the cash outflows.

The fair value of the loan shall be as follows:

© The Institute of Chartered Accountants of India

Date	Outstanding loan	Principal	Interest income @ 6%	Total inflow	Discount factor @ 10%	PV
31 March 20X2	15,00,000	3,00,000	90,000	3,90,000	0.909	3,54,510
31 March 20X3	12,00,000	3,00,000	72,000	3,72,000	0.826	3,07,272
31 March 20X4	9,00,000	3,00,000	54,000	3,54,000	0.751	2,65,854
31 March 20X5	6,00,000	3,00,000	36,000	3,36,000	0.683	2,29,488
31 March 20X6	3,00,000	3,00,000	18,000	3,18,000	0.621	1,97,478
Fair value of the loan						13,54,602

As per Ind AS 19, employee benefits are all forms of consideration given by an entity in exchange for service rendered by employees or for termination of employment. Difference of loan proceeds and present value of the loan (fair value) will be treated as prepaid employee cost irrespective of the fact that employee is not required to give any specific performance against this benefit. This is because employee is required to be in service of the company to continue availing the benefits of concessional rate of interest on housing loan. Practically, once the employee leaves the organisation, they have to repay the outstanding loan because the company provides the loan at concessional rate of interest only to its employees.

Hence, it is an employee benefit given by the company to its employees. This deemed employee cost of ₹ 1,45,398 (15,00,000 – 13,54,602) will be deferred and amortised over the period of loan on straight line basis.

Calculation of amortised cost of loan to employees

Financial year ending on 31 March	Amortised cost (opening balance)	Interest to be recognised @ 10%	Repayment (including interest)	Amortised cost (closing balance)
20X2	13,54,602	1,35,460	3,90,000	11,00,062
20X3	11,00,062	1,10,006	3,72,000	8,38,068
20X4	8,38,068	83,807	3,54,000	5,67,875
20X5	5,67,875	56,788	3,36,000	2,88,663
20X6	2,88,663	29,337*	3,18,000	-

* 2,88,663 x 10% = ₹ 28,866. Difference of ₹ 471 (29,337 – 28,866) is due to approximation in computation.

© The Institute of Chartered Accountants of India

Journal Entries to be recorded at every period end:

1. On 1 April 20X1

Particulars		Dr. Amount (₹)	Cr. Amount (₹)
Loan to employee A/c	Dr.	13,54,602	
Prepaid employee cost A/c	Dr.	1,45,398	
To Bank A/c			15,00,000
(Being loan asset recorded at initial fair value)			

2. On 31 March 20X2

Particulars		Dr. Amount (₹)	Cr. Amount (₹)
Bank A/c	Dr.	3,90,000	
To Finance income A/c (profit and loss) @10%			1,35,460
To Loan to employee A/c			2,54,540
(Being first instalment of repayment of loan accounted for using the amortised cost and effective interest rate @ 10%)			
Employee benefit cost (profit and loss) A/c Dr.		29,080	
To Prepaid employee cost A/c (1,45,398/5)			29,080
(Being amortization of pre-paid employee cost charged to profit and loss as employee benefit cost)			

The Following housing loan balances should appear in the financial statements:

Extracts of Balance sheet of Star Ltd. as at 31 March 20X2

Non-current asset	
Financial asset	
Loan to employee (11,00,062 – 3,72,000 + 1,10,006)	8,38,068
Other non-current asset	
Prepaid employee cost	87,238
Current asset	
Financial asset	
Loan to employee (3,72,000-1,10,006)	2,61,994
Other current asset	
Prepaid employee cost	29,080

© The Institute of Chartered Accountants of India

Deferred tax on temporary differences arising on the above-mentioned account balances (appearing in the balance sheet) should be recognised. However, in the absence of any tax rate in the question no deferred tax has been recognised.

Case Study 2

Pluto Ltd. has purchased a manufacturing plant for ₹ 6 lakhs on 1st April, 20X1. The useful life of the plant is 10 years. On 30th September, 20X3, Pluto temporarily stops using the manufacturing plant because demand has declined. However, the plant is maintained in a workable condition and it will be used in future when demand picks up.

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

Also, the accountant has also stopped charging the depreciation for the rest of period considering the plant as held for sale. The fair value less cost to sell on 30th September, 20X3 and 31st March, 20X4 was ₹ 4 lakhs and ₹ 3.5 lakhs respectively.

The accountant has performed the following working: ₹

Carrying amount on initial classification as held for sale		
Purchase Price of Plant	6,00,000	
Less: Accumulated dep (6,00,000/ 10 Years) x 2.5 years	(1,50,000)	4,50,000
Fair Value less cost to sell as on 30th September, 20X3		4,00,000
The value will be lower of the above two		4,00,000

Balance Sheet extracts as on 31st March, 20X4

Assets	
Current Assets	
Other Current Assets	
Assets classified as held for sale	3,50,000

Analyse whether the above accounting treatment made by the accountant is in compliance with the Ind AS. If not, advise the correct treatment alongwith the necessary workings.

© The Institute of Chartered Accountants of India

Solution:

The above treatment needs to be examined in the light of the provisions given in Ind AS 16 '*Property, Plant and Equipment*' and Ind AS 105 '*Non-current Assets Held for Sale and Discontinued Operations'.*

Para 6 of Ind AS 105 *'Non-current Assets Held for Sale and Discontinued Operations'* states that:

"An entity shall classify a non-current asset (or disposal group) as held for sale if its carrying amount will be recovered principally through a sale transaction rather than through continuing use".

Paragraph 7 of Ind AS 105 states that:

"For this to be the case, the asset (or disposal group) must be available for immediate sale in its present condition subject only to terms that are usual and customary for sales of such assets (or disposal groups) and its sale must be highly probable. Thus, an asset (or disposal group) cannot be classified as a non-current asset (or disposal group) held for sale, if the entity intends to sell it in a distant future".

Further, paragraph 8 of Ind AS 105 states that:

"For the sale to be highly probable, the appropriate level of management must be committed to a plan to sell the asset (or disposal group), and an active programme to locate a buyer and complete the plan must have been initiated. Further, the asset (or disposal group) must be actively marketed for sale at a price that is reasonable in relation to its current fair value. In addition, the sale should be expected to qualify for recognition as a completed sale within one year from the date of classification and actions required to complete the plan should indicate that it is unlikely that significant changes to the plan will be made or that the plan will be withdrawn."

Paragraph 13 of Ind AS 105 states that:

"An entity shall not classify as held for sale a non-current asset (or disposal group) that is to be abandoned. This is because its carrying amount will be recovered principally through continuing use."

Paragraph 14 of Ind AS 105 states that:

"An entity shall not account for a non-current asset that has been temporarily taken out of use as if it had been abandoned."

Paragraph 55 of Ind AS 16 states that:

"Depreciation does not cease when the asset becomes idle or is retired from active use unless the asset is fully depreciated."

Going by the guidance given above,

© The Institute of Chartered Accountants of India

The Accountant of Pluto Ltd. has treated the plant as held for sale and measured it at the fair value less cost to sell. Also, the depreciation has not been charged thereon since the date of classification as held for sale which is not correct and not in accordance with Ind AS 105 and Ind AS 16.

Accordingly, the manufacturing plant should neither be treated as abandoned asset nor as held for sale because its carrying amount will be principally recovered through continuous use. Pluto Ltd. shall not stop charging depreciation or treat the plant as held for sale because its carrying amount will be recovered principally through continuing use to the end of their economic life.

The working of the same for presenting in the balance sheet is given as below:

Calculation of carrying amount as on 31st March, 20X4	
Purchase Price of Plant	6,00,000
Less: Accumulated depreciation (6,00,000/ 10 Years) x 3 Years	(1,80,000)
	4,20,000
Less: Impairment loss	(70,000)
	3,50,000

Balance Sheet extracts as on 31st March, 20X4

Assets	
Non-Current Assets	
Property, Plant and Equipment	3,50,000

Working Note:

Fair value less cost to sell of the Plant = ₹ 3,50,000

Value in Use (not given) or = Nil (since plant has temporarily not been used for manufacturing due to decline in demand)

Recoverable amount = higher of above i.e. ₹ 3,50,000

Impairment loss = Carrying amount – Recoverable amount

Impairment loss = ₹ 4,20,000 - ₹ 3, 50,000 = ₹ 70,000.

Case Study 3

On 5th April, 20X2, fire damaged a consignment of inventory at one of the Jupiter's Ltd.'s warehouse. This inventory had been manufactured prior to 31st March, 20X2 costing ₹ 8 lakhs. The net realisable value of the inventory prior to the damage was estimated at ₹ 9.60 lakhs. Because of the damage caused to the consignment of inventory, the company was required to

© The Institute of Chartered Accountants of India

spend an additional amount of ₹ 2 lakhs on repairing and re-packaging of the inventory. The inventory was sold on 15th May, 20X2 for proceeds of ₹ 9 lakhs.

The accountant of Jupiter Ltd treats this event as an adjusting event and adjusted this event of causing the damage to the inventory in its financial statement and accordingly re-measures the inventories as follows: *₹ lakhs*

	₹ lakhs
Cost	*8.00*
Net realisable value (9.6 -2)	*7.60*
Inventories (lower of cost and net realisable value)	*7.60*

Analyse whether the above accounting treatment made by the accountant in regard to financial year ending on 31.0.20X2 is in compliance of the Ind AS. If not, advise the correct treatment alongwith working for the same.

Solution:

The above treatment needs to be examined in the light of the provisions given in Ind AS 10 *'Events after the Reporting Period'* and *Ind AS 2 'Inventories'*.

Para 3 of Ind AS 10 *'Events after the Reporting Period'* defines *"Events after the reporting period are those events, favourable and unfavourable, that occur between the end of the reporting period and the date when the financial statements are approved by the Board of Directors in case of a company, and, by the corresponding approving authority in case of any other entity for issue. Two types of events can be identified:*

(a) those that provide evidence of conditions that existed at the end of the reporting period (adjusting events after the reporting period); and

(b) those that are indicative of conditions that arose after the reporting period (non-adjusting events after the reporting period).

Further, paragraph 10 of Ind AS 10 states that:

"An entity shall not adjust the amounts recognised in its financial statements to reflect non-adjusting events after the reporting period".

Further, paragraph 6 of Ind AS 2 defines:

"Net realisable value is the estimated selling price in the ordinary course of business less the estimated costs of completion and the estimated costs necessary to make the sale".

Further, paragraph 9 of Ind AS 2 states that:

"Inventories shall be measured at the lower of cost and net realisable value".

© The Institute of Chartered Accountants of India

Accountant of Jupiter Ltd. has re-measured the inventories after adjusting the event in its financial statement which is not correct and nor in accordance with provision of Ind AS 2 and Ind AS 10.

Accordingly, the event causing the damage to the inventory occurred after the reporting date and as per the principles laid down under Ind AS 10 '*Events After the Reporting Date'* is a non-adjusting event as it does not affect conditions at the reporting date. Non-adjusting events are not recognised in the financial statements, but are disclosed where their effect is material.

Therefore, as per the provisions of Ind AS 2 and Ind AS 10, the consignment of inventories shall be recorded in the Balance Sheet at a value of ₹ 8 Lakhs calculated below: *₹' lakhs*

Cost	8.00
Net realisable value	9.60
Inventories (lower of cost and net realisable value)	8.00

Case Study 4

On 1st April, 20X1, Sun Ltd. has acquired 100% shares of Earth Ltd. for ₹ 30 lakhs. Sun Ltd. has 3 cash-generating units A, B and C with fair value of ₹ 12 lakhs, ₹ 8 lakhs and ₹ 4 lakhs respectively. The company recognizes goodwill of Rs 6 lakhs that relates to CGU 'C' only.

During the financial year 20X2-20X3, the CFO of the company has a view that there is no requirement of any impairment testing for any CGU since their recoverable amount is comparatively higher than the carrying amount and believes there is no indicator of impairment.

Analyse whether the view adopted by the CFO of Sun Ltd is in compliance of the Ind AS. If not, advise the correct treatment in accordance with relevant Ind AS

Solution

The above treatment needs to be examined in the light of the provisions given in Ind AS 36: Impairment of Assets.

Para 9 of Ind AS 36 *'Impairment of Assets'* states that *"An entity shall assess at the end of each reporting period whether there is any indication that an asset may be impaired. If any such indication exists, the entity shall estimate the recoverable amount of the asset."*

Further, paragraph 10(b) of Ind AS 36 states that:

"Irrespective of whether there is any indication of impairment, an entity shall also test goodwill acquired in a business combination for impairment annually."

Sun Ltd has not tested any CGU on account of not having any indication of impairment is partially correct i.e. in respect of CGU A and B but not for CGU C. Hence, the treatment made by the Company is not in accordance with Ind AS 36.

© The Institute of Chartered Accountants of India

Accordingly, impairment testing in respect of CGU A and B are not required since there are no indications of impairment. However, Sun Ltd shall test CGU C irrespective of any indication of impairment annually as the goodwill acquired on business combination is fully allocated to CGU 'C'.

Case Study 5

Deepak started a new company Softbharti Pvt. Ltd. with Iktara Ltd. wherein investment of 55% is done by Iktara Ltd. and rest by Deepak. Voting powers are to be given as per the proportionate share of capital contribution. The new company formed was the subsidiary of Iktara Ltd. with two directors, and Deepak eventually becomes one of the directors of company. A consultant was hired and he charged ₹ 30,000 for the incorporation of company and to do other necessary statuary registrations. ₹ 30,000 is to be charged as an expense in the books after incorporation of company. The company, Softbharti Pvt. Ltd. was incorporated on 1st April 20X1.

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

An accountant who was hired at the time of company's incorporation, has prepared the draft financials of Softbharti Pvt. Ltd. for the year ending 31st March, 20X2 as follows:

Statement of Profit and Loss

Particulars	Amount (₹)
Revenue from operations	10,00,000
Other Income	1,00,000
Total Revenue (a)	**11,00,000**
Expenses:	
Purchase of stock in trade	5,00,000
(Increase)/Decrease in stock in trade	(50,000)
Employee benefits expense	1,75,000
Depreciation	30,000
Other expenses	90,000
Total Expenses (b)	**7,45,000**
Profit before tax (c) = (a)-(b)	**3,55,000**
Current tax	1,06,500
Deferred tax	6,000
Total tax expense (d)	**1,12,500**
Profit for the year (e) = (c) – (d)	**2,42,500**

© The Institute of Chartered Accountants of India

Balance Sheet

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

Additional information of Softbharti Pvt Ltd.:

i. Deferred tax liability of ₹ 6,000 is created due to following temporary difference:

Difference in depreciation amount as per Income tax and Accounting profit

ii. There is only one property, plant and equipment in the company, whose closing balance as at 31st March, 20X2 is as follows:

Asset description	As per Books	As per Income tax
Property, plant and equipment	₹ 1,00,000	₹ 80,000

© The Institute of Chartered Accountants of India

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

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

v. After the reporting period, the directors have recommended dividend of ₹ 15,000 for the year ending 31st March, 20X2 which has been deducted from reserves and surplus. Dividend payable of ₹ 15,000 has been grouped under 'other current liabilities' alongwith other financial liabilities.

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

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

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

ix. Current investment of ₹ 30,000 is in shares of a company which was done with the purpose of trading; current investment has been carried at cost in the financial statements. The fair value of current investment in this case is ₹ 50,000 as at 31st March, 20X2.

x. Actuarial gain on employee benefit measurements of ₹ 1,000 has been omitted in the financials of Softbharti private limited for the year ending 31st March, 20X2.

The financial statements for financial year 20X1-20X2 have not been yet approved.

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

Solution

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

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

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

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

© The Institute of Chartered Accountants of India

STATEMENT OF PROFIT AND LOSS
for the year ended 31st March, 20X2

Particulars	Amount (₹)
Revenue from operations	10,00,000
Other Income (1,00,000 + 20,000) (refer note -1)	1,20,000
Total Revenue	**11,20,000**
Expenses:	
Purchase of stock in trade	5,00,000
(Increase) / Decrease in stock in trade	(50,000)
Employee benefits expense	1,75,000
Depreciation	30,000
Other expenses	90,000
Total Expenses	**7,45,000**
Profit before tax	**3,75,000**
Current tax	1,25,700
Deferred tax (W.N.1)	4,800
Total tax expense	**1,30,500**
Profit for the year (A)	**2,44,500**
OTHER COMPREHENSIVE INCOME	
Items that will not be reclassified to Profit or Loss:	
Remeasurements of net defined benefit plans	**1,000**
Tax liabilities relating to items that will not be reclassified to Profit or Loss	
Remeasurements of net defined benefit plans (tax) [1000 x 30%]	(300)
Other Comprehensive Income for the period (B)	**700**
Total Comprehensive Income for the period (A+B)	**2,45,200**

BALANCE SHEET
as at 31st March, 20X2

Particulars	(₹)
ASSETS	
Non-current assets	
Property, plant and equipment	1,00,000
Financial assets	

© The Institute of Chartered Accountants of India

Other financial assets (Long-term loans and advances)	40,000
Other non-current assets (capital advances) (refer note-2)	50,000
Current assets	
Inventories	80,000
Financial assets	
Investments (30,000 + 20,000) (refer note -1)	50,000
Trade receivables	55,000
Cash and cash equivalents/Bank	1,15,000
Other financial assets (Interest receivable from trade receivables)	51,000
TOTAL ASSETS	**5,41,000**
EQUITY AND LIABILITIES	
Equity	
Equity share capital	1,00,000
Other equity	2,45,200
Non-current liabilities	
Provision (25,000 – 1,000)	24,000
Deferred tax liabilities (4800 + 300)	5,100
Current liabilities	
Financial liabilities	
Trade payables	11,000
Other financial liabilities (Refer note 5)	15,000
Other current liabilities (Govt. statuary dues) (Refer note 3)	15,000
Current tax liabilities	1,25,700
TOTAL EQUITY AND LIABILITIES	**5,41,000**

STATEMENT OF CHANGES IN EQUITY

For the year ended 31st March, 20X2

A. EQUITY SHARE CAPITAL

	Balance (₹)
As at 31st March, 20X1	-
Changes in equity share capital during the year	1,00,000
As at 31st March, 20X2	1,00,000

© The Institute of Chartered Accountants of India

B. OTHER EQUITY

	Reserves & Surplus
	Retained Earnings (₹)
As at 31st March, 20X1	-
Profit for the year	2,44,500
Other comprehensive income for the year	700
Total comprehensive income for the year	2,45,200
Less: Dividend on equity shares (refer note – 4)	-
As at 31st March, 20X2	2,45,200

DISCLOSURE FORMING PART OF FINANCIAL STATEMENTS:

Proposed dividend on equity shares is subject to the approval of the shareholders of the company at the annual general meeting and not recognized as liability as at the Balance Sheet date. (refer note 4)

Notes:

1. Current investment are held for the purpose of trading. Hence, it is a financial asset classified as FVTPL. Any gain in its fair value will be recognised through profit or loss. Hence, ₹ 20,000 (₹ 50,000 – ₹ 30,000) increase in fair value of financial asset will be recognised in profit and loss. However, it will attract deferred tax liability on increased value (Refer W.N).
2. Assets for which the future economic benefit is the receipt of goods or services, rather than the right to receive cash or another financial asset, are not financial assets.
3. Liabilities for which there is no contractual obligation to deliver cash or other financial asset to another entity, are not financial liabilities.
4. As per Ind AS 10, 'Events after the Reporting Period', If dividends are declared after the reporting period but before the financial statements are approved for issue, the dividends are not recognized as a liability at the end of the reporting period because no obligation exists at that time. Such dividends are disclosed in the notes in accordance with Ind AS 1, Presentation of Financial Statements.
5. Other current financial liabilities:

	(₹)
Balance of other current liabilities as per financial statements	45,000
Less: Dividend declared for FY 20X1 – 20X2 (Note – 4)	(15,000)
Reclassification of government statuary dues payable to 'other current liabilities'	(15,000)
Closing balance	15,000

© The Institute of Chartered Accountants of India

Working Note:

Calculation of deferred tax on temporary differences as per Ind AS 12 for financial year 20X1 – 20X2

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

Case Study 6

Mumbai Challengers Ltd., a listed entity, is a sports organization owning several cricket and hockey teams. The issues below pertain to the reporting period ending 31 March 20X2.

(a) Owing to the proposed schedules of Indian Hockey League as well as Cricket Premier Tournament, Mumbai Challengers Ltd. needs a new stadium to host the sporting events. This stadium will form a part of the Property, Plant and Equipment of the company. Mumbai Challengers Ltd. began the construction of the stadium on 1 December, 20X1. The construction of the stadium was completed in 20X2-20X3. Costs directly related to the construction amounted to ₹ 140 crores in December 20X1. Thereafter, ₹ 350 crores have been incurred per month until the end of the financial year. The company has not taken any specific borrowings to finance the construction of the stadium, although it has incurred finance costs on its regular overdraft during the period, which were avoidable had the stadium not been constructed. Mumbai Challengers Ltd. has calculated that the weighted average cost of the borrowings for the period 1 December 20X1 to 31 March 20X2 amounted to 15% per annum on an annualized basis.

The company seeks advice on the treatment of borrowing costs in its financial statements for the year ending 31 March 20X2.

(b) Mumbai Challengers Ltd. acquires and sells players' registrations on a regular basis. For a player to play for its team, Mumbai Challengers Ltd. must purchase registrations for that player. These player registrations are contractual obligations between the player and the company. The costs of acquiring player registrations include transfer fees, league levy fees, and player agents' fees incurred by the club.

At the end of each season, which happens to also be the reporting period end for Mumbai Challengers Ltd., the club reviews its contracts with the players and makes decisions as to whether they wish to sell/transfer any players' registrations. The company actively markets

© The Institute of Chartered Accountants of India

these registrations by circulating with other clubs a list of players' registrations and their estimated selling price. Players' registrations are also sold during the season, often with performance conditions attached. In some cases, it becomes clear that a player will not play for the club again because of, for example, a player sustaining a career threatening injury or being permanently removed from the playing squad for any other reason. The playing registrations of certain players were sold after the year end, for total proceeds, net of associated costs, of ₹ 175 crores. These registrations had a net book value of ₹ 49 crores.

Mumbai Challengers Ltd. seeks your advice on the treatment of the acquisition, extension, review and sale of players' registrations in the circumstances outlined above.

(c) Mumbai Challengers Ltd. measures its stadiums in accordance with the revaluation model. An airline company has approached the directors offering ₹ 700 crores for the property naming rights of all the stadiums for five years. Three directors are on the management boards of both Mumbai Challengers Ltd. and the airline. Additionally, statutory legislations regulate the financing of both the cricket and hockey clubs. These regulations prevent contributions to the capital from a related party which 'increases equity without repayment in return'. Failure to adhere to these legislations could lead to imposition of fines and withholding of prize money.

Mumbai Challengers Ltd. wants to know how to take account of the naming rights in the valuations of the stadium and the potential implications of the financial regulations imposed by the legislations.

Solution:

(a) Borrowing Costs

As per Ind AS 23 *Borrowing Costs*, an entity shall capitalize borrowing costs that are directly attributable to the acquisition, construction or production of a qualifying asset (i.e. an asset that necessarily takes a substantial period of time to get ready for its intended use or sale) as part of the cost of that asset. The borrowing costs that are directly attributable to the acquisition, construction or production of a qualifying asset are those borrowing costs that would have been avoided if the expenditure on the qualifying asset had not been made. To the extent that an entity borrows funds generally and uses them for the purpose of obtaining a qualifying asset, the entity shall determine the amount of borrowing costs eligible for capitalization by applying a capitalization rate to the expenditures on that asset. The capitalization rate shall be the weighted average of the borrowing costs applicable to all borrowings of the entity that are outstanding during the period.

The capitalization rate of the borrowings of Mumbai Challengers Ltd. during the period of construction is 15% per annum (as given in the question), and therefore, the total amount of borrowing costs to be capitalized is the expenditures incurred on the asset multiplied by the capitalization rate, which is as under:

© The Institute of Chartered Accountants of India

Particulars	₹ in crores
Costs incurred in December 20X1: (₹ 140 crores x 15% x 4/12)	7.000
Costs incurred in January 20X2: (₹ 350 crores x 15% x 3/12)	13.125
Costs incurred in February 20X2: (₹ 350 crores x 15% x 2/12)	8.750
Costs incurred in March 20X2: (₹ 350 crores x 15% x 1/12)	4.375
Borrowing Costs to be capitalized in 20X1-X2	**33.250**

OR

Weighted average carrying amount of the stadium during 20X1-X2 is:

₹ (140 + 490 + 840 + 1,190) crores/4 = ₹ 665 crores

Applying the weighted average rate of borrowings of 15% per annum, the borrowing cost to be capitalized is computed as:

₹ 665 crores x (15% x 4/12) = ₹ 33.25 crores

(b) Players' Registrations

Acquisition

As per Ind AS 38 *Intangible Assets*, an entity should recognize an intangible asset where it is probable that the expected future economic benefits that are attributable to the asset will flow to the entity and the cost of the asset can be measured reliably. Accordingly, the **costs** associated with the acquisition of players' registrations would need to be **capitalized which would be the amount of cash or cash equivalent paid or the fair value of other consideration given to acquire such registrations**. In line with Ind AS 38 *Intangible Assets*, costs would include transfer fees, league levy fees, and player agents' fees incurred by the club, along with other directly attributable costs, if any. Amounts capitalized would be fully amortized over the period covered by the player's contract.

Sale of registrations

Player registrations would be classified as assets held for sale under Ind AS 105 *Non-Current Assets Held for Sale and Discontinued Operations* when their carrying amount is expected to be recovered principally through a sale transaction and a sale is considered to be highly probable. To consider a sale to be 'highly probable', the assets (in this case, player registrations) should be actively marketed for sale at a price that is reasonable in relation to its current fair value. In the given case, it would appear that the management is committed to a plan to sell the registration, that the asset is available for immediate sale and that an active plan to locate a buyer is already in place by circulating clubs. Ind AS 105 stipulates that it should be unlikely that the plan to sell the registrations would be significantly changed or withdrawn. To fulfil this requirement, it would be prudent if only

© The Institute of Chartered Accountants of India

those registrations are classified as held for sale where unconditional offers have been received prior to the reporting date.

Once the conditions for classifying assets as held for sale in accordance with Ind AS 105 have been fulfilled, the player registrations would be stated at lower of carrying amount and fair value less costs to sell, with the carrying amount stated in accordance with Ind AS 38 prior to application of Ind AS 105, subjected to impairment, if any.

Profits and losses on sale of players' registrations would be computed by deducting the carrying amount of the players' registrations from the fair value of the consideration receivable, net of transactions costs. In case a portion of the consideration is receivable on the occurrence of a future performance condition (i.e. contingent consideration), this amount would be recognized in the Statement of Profit and Loss only when the conditions are met.

The players registrations disposed of, subsequent to the year end, for ₹ 175 crores, having a corresponding book value of ₹ 49 crores would be disclosed as a non-adjusting event in accordance with Ind AS 10 *Events after the Reporting Period*.

Impairment review

Ind AS 36 *Impairment of Assets* requires companies to **annually test their assets for impairment**. An asset is said to be impaired if the carrying amount of the asset exceeds its recoverable amount. The recoverable amount is higher of the asset's fair value less costs to sell and its value in use (which is the present value of future cash flows expected to arise from the use of the asset). In the given scenario, it is not easy to determine the value in use of any player in isolation as that player cannot generate cash flows on his/her own unless via a sale transaction or an insurance recovery. Whilst any individual player cannot really be separated from the single cash-generating unit (CGU), being a cricket team or a hockey team in the instant case, there may be certain instances where a player is taken out of the CGU when it becomes clear that he/she will not play for the club again. If such circumstances arise, the **carrying amount of the player should be assessed against the best estimate of the player's fair value less any costs to sell and an impairment charge should be recognized in the profit or loss**, which reflects any loss arising.

(c) Valuation of stadiums

In terms of Ind AS 113 *Fair Value Measurement*, stadiums would be valued at the **price which would be received to sell the asset in an orderly transaction between market participants** at the measurement date (i.e. exit price). The price would be the one which **maximizes the value of the asset** or the group of assets using the principle of the highest and best use. The price would essentially use Level 2 inputs which are inputs other than quoted market prices included within Level 1 which are observable for the asset or liability, either directly or indirectly. Property naming rights present complications when valuing property. The status of the property indicates its suitability for inviting sponsorship attached

© The Institute of Chartered Accountants of India

to its name. It has nothing to do with the property itself but this can be worth a significant amount. Therefore, Mumbai Challengers Ltd. could include the property naming rights in the valuation of the stadium and write it off over three years.

Ind AS 24 *Related Party Disclosures* lists the criteria for two entities to be treated as related parties. Such criteria include being members of the same group or where a person or a close member of that person's family is related to a reporting entity if that person has control or joint control over the reporting entity. Ind AS 24 deems that parties are not related simply because they have a director or a key manager in common. In this case, there are three directors in common and in the absence of any information to the contrary, it appears as though the entities are not related. However, the regulator will need to establish whether the sponsorship deal is a related party transaction for the purpose of the financial control provisions. There would need to be demonstrated that the airline may be expected to influence, or be influenced by, the club or a related party of the club. If the deal is deemed to be a related party transaction, the regulator will evaluate whether the sponsorship is at fair value or not.

Case Study 7

(a) Neelanchal Gas Refinery Ltd. (hereinafter referred to as Neelanchal), a listed company, is involved in the production and trading of natural gas and oil. Neelanchal jointly owns an underground storage facility with another entity, Seemanchal Refineries Ltd. (hereinafter referred to as Seemanchal). Both the companies are engaged in extraction of gas from offshore gas fields, which they own and operate independently of each other. Neelanchal owns 60% of the underground facility and Seemanchal owns 40%. Both the companies have agreed to share services and costs accordingly, with decisions relating to the storage facility requiring unanimous agreement of the parties. The underground facility is pressurised so that the gas is pushed out when extracted. When the gas pressure is reduced to a certain level, the remaining gas is irrecoverable and remains in the underground storage facility until it is decommissioned. As per the laws in force, the storage facility should be decommissioned at the end of its useful life.

Neelanchal seeks your advice on the treatment of the agreement with Seemanchal as well as the accounting for the irrecoverable gas.

(b) Neelanchal has entered into a ten-year contract with Uttaranchal Refineries Pvt. Ltd. (hereinafter referred to as Uttaranchal) for purchase of natural gas. Neelanchal has paid an advance to Uttaranchal equivalent to the total quantity of gas contracted for ten years based on the forecasted price of gas. This advanced amount carries interest at the rate of 12.5% per annum, which is settled by Uttaranchal way of supply of extra gas. The contract requires fixed quantities of gas to be supplied each month. Additionally, there is a price adjustment mechanism in the contract whereby the difference between the forecasted price of gas and the prevailing market price is settled in cash on a quarterly

© The Institute of Chartered Accountants of India

basis. If Uttaranchal does not deliver the gas as agreed, Neelanchal has the right to claim compensation computed at the current market price of the gas.

Neelanchal wants to account for the contract with Uttaranchal in accordance with Ind AS 109 *Financial Instruments* and seeks your inputs in this regard.

Solution

(a) Joint Arrangement

As per Ind AS 111 *Joint Arrangements*, a joint arrangement is an arrangement of which two or more parties have joint control. Joint control is the contractually agreed sharing of control of an arrangement, which exists only when decisions about the relevant activities require the unanimous consent of the parties sharing control. The structure and form of the arrangement determines the nature of the relationship. However, irrespective of the purpose, structure or form of the arrangement, the classification of joint arrangements depends upon the parties' rights and obligations arising from the arrangement. Accordingly, a joint arrangement could be classified as a joint operation or as a joint venture. A joint arrangement which is NOT structured through a separate vehicle is a joint operation. In such cases, the contractual arrangement establishes the parties' rights and obligations. A joint operator accounts for the assets, liabilities, revenues and expenses relating to its involvement in a joint operation in accordance with the relevant Ind AS. Based on the information provided, the arrangement with Seemanchal Refineries Ltd. is a joint operation as no separate vehicle is formed and the companies have agreed to share services and costs with decisions regarding the storage facility requiring unanimous agreement of the parties. Neelanchal Gas Refinery Ltd. should recognize its share of the asset as Property, Plant and Equipment.

As per Para 16 of Ind AS 16 Property, Plant and Equipment, the cost of an item of property, plant and equipment comprises the initial estimate of the costs of dismantling and removing the item and restoring the site on which it is located. Ind AS 37 *Provisions, Contingent Liabilities and Contingent Assets* provides guidance on measuring decommissioning, restoration and similar liabilities. Para 45 of Ind AS 37 provides that where the effect of the time value of money is material, the amount of a provision shall be the present value of the expenditures expected to be required to settle the obligation. Thus, costs incurred by an entity in respect of obligations for dismantling, removing and restoring the site on which an item of property, plant and equipment is situated are recognized and measured in accordance with Ind AS 16 and Ind AS 37, with the journal entry being as under:

Property, Plant and Equipment	Dr.	xxx	
To Provision for Dismantling, Removal and Restoration			xxx

Neelanchal Gas Refinery Ltd. should recognize 60% of the cost of decommissioning of the underground storage facility. However, in line Para 29 of Ind AS 37 where an entity is jointly

© The Institute of Chartered Accountants of India

and severally liable for an obligation, **the part of the obligation that is expected to be met by other parties is treated as a contingent liability**. Accordingly, Neelanchal Gas Refinery Ltd. should also disclose 40% of the cost of decommissioning of the underground facility as a contingent liability, should there arise future events that prevent Seemanchal Refineries Ltd. from fulfilling its obligations under the arrangement.

As per Ind AS 16, Property, Plant and Equipment are tangible items that:

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

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

Thus, Neelanchal Gas Refinery Ltd. should classify and account for its share of irrecoverable gas as property, plant and equipment, as the irrecoverable gas is necessary for the storage facility to perform its function. Therefore, the **irrecoverable gas, being a part of the storage facility, should be capitalized as a component of the storage facility asset**, and should be depreciated to its residual value over the life of the storage facility. However, if the gas is recoverable in full upon decommissioning of the storage facility, then depreciation against the irrecoverable gas component will be recorded only if the estimated residual value of the gas decreases below cost during the life of the facility. Upon decommissioning of the storage facility, when the cushion gas is extracted and sold, the sale of irrecoverable gas is accounted as a disposal of an item of property, plant and equipment in accordance with Ind AS 16 and the resulting gain or loss is recognized in the Statement of Profit and Loss. The natural gas in excess of the irrecoverable gas which is injected into the facility would be treated as inventory in accordance with Ind AS 2 *Inventories*.

(b) Contract with Uttaranchal Refineries Pvt. Ltd.

As per para 2.4 of Ind AS 109 *Financial Instruments,* this standard applies to those contracts to buy or sell a non-financial item that can be settled net in cash or another financial instrument, or by exchanging financial instruments, as if the contracts were financial instruments, **with the exception** of contracts that were entered into and continue to be held for the purpose of the receipt or delivery of a non-financial item in accordance with the entity's expected purchase, sale or usage requirements (i.e. own use contracts). This contract will result in physical delivery of the commodity i.e. extra gas.

Para 2.5 of Ind AS 109 further provides that a contract to buy or sell a non-financial item that can be settled net in cash or another financial instrument, or by exchanging financial instruments, as if the contract was a financial instrument, may be irrevocably designated as measured at fair value through profit or loss even if it was entered into for the purpose of the receipt or delivery of a non-financial item in accordance with the entity's expected purchase, sale or usage requirements. This designation is available only at inception of the contract and only if it eliminates or significantly reduces a recognition inconsistency

© The Institute of Chartered Accountants of India

(sometimes referred to as an 'accounting mismatch') that would otherwise arise from not recognising that contract because it is excluded from the scope of this Standard.

There are various ways in which a contract to buy or sell a non-financial item can be settled net in cash or another financial instrument or by exchanging financial instruments. These include:

(a) when the terms of the contract permit either party to settle it net in cash or another financial instrument or by exchanging financial instruments;

(b) when the ability to settle net in cash or another financial instrument, or by exchanging financial instruments, is not explicit in the terms of the contract, but the entity has a practice of settling similar contracts net in cash or another financial instrument or by exchanging financial instruments (whether with the counterparty, by entering into offsetting contracts or by selling the contract before its exercise or lapse);

(c) when, for similar contracts, the entity has a practice of taking delivery of the underlying and selling it within a short period after delivery for the purpose of generating a profit from short-term fluctuations in price or dealer's margin; and

(d) when the non-financial item that is the subject of the contract is readily convertible to cash.

A written option to buy or sell a non-financial item, such as a commodity, that can be settled net in cash or another financial instrument, or by exchanging financial instruments, is within the scope of Ind AS 109. Such a contract is accounted as a derivative. Such a contract cannot be entered into for the purpose of the receipt or delivery of the non-financial item in accordance with the entity's expected purchase, sale or usage requirements. Judgment would be required in this area as net settlements caused by unique events beyond management's control may not necessarily prevent the entity from applying the 'own use' exemption to all similar contracts.

In the given case, the contract with Uttaranchal Refineries Pvt. Ltd. will result in physical delivery of extra gas (which is a commodity and not cash, or a financial instrument) for the use of Neelanchal Gas Refinery Ltd. Accordingly, it appears that this contract would be an own use contract falling outside the scope of Ind AS 109 and therefore, would be treated as an executory contract. However, arguments could be placed that the contract is net settled due to the penalty mechanism requiring Uttaranchal Refineries Pvt. Ltd. to compensate Neelanchal Gas Refinery Ltd. at the current prevailing market price. Further, if natural gas is readily convertible into cash at the location of delivery, the contract could be considered net settled. Additionally, if there is volume flexibility, the contract could be regarded as a written option which falls within the scope of Ind AS 109.

However, the contract will probably continue to be regarded as 'own use' as long as it has been entered into and continues to be held for expected counterparties' sale / usage requirements. Additionally, the entity has not irrevocably designated the contract as measured at fair value through profit or loss, thus emphasizing the 'own use' designation.

© The Institute of Chartered Accountants of India

TEST YOUR KNOWLEDGE

Questions

1. Venus Ltd. is a multinational entity that owns three properties. All three properties were purchased on 1st April, 20X1. The details of purchase price and market values of the properties are given as follows:

Particulars	Property 1	Property 2	Property 3
	Factory	Factory	Let-Out
Purchase price	15,000	10,000	12,000
Market value 31.03.20X2	16,000	11,000	13,500
Life	10 Years	10 Years	10 Years
Subsequent Measurement	Cost Model	Revaluation Model	Revaluation Model

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

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

Required:

Analyse whether the accounting policies adopted by the Venus Ltd. in relation to these properties is in accordance with Ind AS. If not, advise the correct treatment alongwith working for the same.

2. On 1st January, 20X2, Sun Ltd. was notified that a customer was taking legal action against the company in respect of a financial losses incurred by the customer. Customer alleged that the financial losses were caused due to supply of faulty products on 30th September, 20X1 by the Company. Sun Ltd. defended the case but considered, based on the progress of the case up to 31st March, 20X2, that there was a 75% probability they would have to pay damages of ₹ 10 lakhs to the customer.

However, the accountant of Sun Ltd. has not recorded this transaction in its financial statement as the case is not yet finally settled. The case was ultimately settled against the company resulting in to payment of damages of ₹ 12 lakhs to the customer on 15th May, 20X2. The financials have been authorized by the Board of Directors in its meeting held on 18th May, 20X2.

© The Institute of Chartered Accountants of India

Analyse whether the above accounting treatment made by the accountant is in compliance of the Ind AS. If not, advise the correct treatment along with working for the same.

3. Mercury Ltd. is an entity engaged in plantation and farming on a large scale diversified across India. On 1st April, 20X1, the company has received a government grant for ₹ 10 lakhs subject to a condition that it will continue to engage in plantation of eucalyptus tree for a coming period of five years. Eucalyptus trees are not considered as bearer plant in this case.

   The management has a reasonable assurance that the entity will comply with condition of engaging in the plantation of eucalyptus tree for specified period of five years and accordingly it recognises proportionate grant for ₹ 2 lakhs in Statement of Profit and Loss as income following the principles laid down under *Ind AS 20 Accounting for Government Grants and Disclosure of Government Assistance*.

   Analyse whether the above accounting treatment made by the management is in compliance of the Ind AS. If not, advise the correct treatment alongwith working for the same.

4. Mercury Ltd. has sold goods to Mars Ltd. at a consideration of ₹ 10 lakhs, the receipt of which receivable in three equal installments of ₹ 3,33,333 over a two year period (receipts on 1st April, 20X1, 31st March, 20X2 and 31st March, 20X3).

   The company is offering a discount of 5 % (i.e. ₹ 50,000) if payment is made in full at the time of sale. The sale agreement reflects an implicit interest rate of 5.36% p.a.

   The total consideration to be received from such sale is at ₹ 10 Lakhs and hence, the management has recognised the revenue from sale of goods for ₹ 10 lakhs.

   Analyse whether the above accounting treatment made by the accountant is in compliance of the Ind AS. If not, advise the correct treatment along with working for the same.

5. Master Creator Private Limited (a subsidiary of listed company) is an Indian company to whom Ind AS are applicable. Following draft balance sheet is prepared by the accountant for year ending 31st March 20X2.

Balance Sheet of Master Creator Private Limited as at 31st March, 20X2

Particulars	₹
ASSETS	
Non-current assets	
Property, plant and equipment	85,37,500
Financial assets	
Other financial assets (Security deposits)	4,62,500

© The Institute of Chartered Accountants of India

Other non-current assets (capital advances)	17,33,480
Deferred tax assets	2,54,150
Current assets	
Trade receivables	7,25,000
Inventories	5,98,050
Financial assets	
Investments	55,000
Other financial assets	2,17,370
Cash and cash equivalents	1,16,950
TOTAL ASSETS	**1,27,00,000**
EQUITY AND LIABILITIES	
Equity share capital	10,00,000
Non-current liabilities	
Other Equity	25,00,150
Deferred tax liability	4,74,850
Borrowings	64,00,000
Long term provisions	5,24,436
Current liabilities	
Financial liabilities	
Other financial liabilities	2,00,564
Trade payables	6,69,180
Current tax liabilities	9,30,820
TOTAL EQUITY AND LIABILITIES	**1,27,00,000**

Additional Information:

1. On 1st April 20X1, 8% convertible loan with a nominal value of ₹ 64,00,000 was issued by the entity. It is redeemable on 31st March 20X5 also at par. Alternatively, it may be converted into equity shares on the basis of 100 new shares for each ₹ 200 worth of loan.

   An equivalent loan without the conversion option would have carried interest at 10%. Interest of ₹ 5,12,000 has already been paid and included as a finance cost.

   Present Value (PV) rates are as follows:

© The Institute of Chartered Accountants of India

Year End	@ 8%	@ 10%
1	0.93	0.91
2	0.86	0.83
3	0.79	0.75
4	0.73	0.68

2. After the reporting period, the board of directors have recommended dividend of ₹ 50,000 for the year ending 31st March, 20X1. However, the same has not been yet accounted by the company in its financials.

3. 'Other current financial liabilities' consists of the following:

Particulars	Amount (₹)
Wages payable	21,890
Salary payable	61,845
TDS payable	81,265
Interest accrued on trade payables	35,564

4. Property, Plant and Equipment consists following items:

Particulars	Amount (₹)	Remarks
Building	37,50,250	It is held for administration purposes
Land	15,48,150	It is held for capital appreciation
Vehicles	12,37,500	These are used as the conveyance for employees
Factory premises	20,01,600	The construction was started on 31st March 20X2 and consequently no depreciation has been charged on it. The construction activities will continue to happen, and it will take 2 years to complete and be available for use.

5. The composition of 'other current financial assets' is as follows:

Particulars	Amount (Rs.)
Interest accrued on bank deposits	57,720
Prepaid expenses	90,000
Royalty receivable from dealers	69,650

6. Current Investments consist of securities held for trading which are carried at fair value through profit & loss. Investments were purchased on 1st January,20X2 at

© The Institute of Chartered Accountants of India

₹ 55,000 and accordingly are shown at cost as at 31st March 20X2. The fair value of said investments as on 31st March 20X2 is ₹ 60,000.

7. Trade payables and Trade receivables are due within 12 months.
8. There has been no changes in equity share capital during the year.
9. Entity has the intention to set off a deferred tax asset against a deferred tax liability as they relate to income taxes levied by the same taxation authority and the entity has a legally enforceable right to set off taxes.
10. Other Equity consists retained earnings only. The opening balance of retained earnings was ₹ 21,25,975 as at 1st April 20X1.
11. No dividend has been actually paid by company during the year.
12. Assume that the deferred tax impact, if any on account of above adjustments is correctly calculated in financials.

Being Finance & Accounts manager, you are required to identify the errors and misstatements if any in the balance sheet of Master Creator Private Limited and prepare corrected balance sheet with details on the face of the balance sheet i.e. no need to prepare notes to accounts, after considering the additional information. Provide necessary explanations/workings for the treated items, wherever necessary.

6. HIM Limited having net worth of ₹ 250 crores is required to adopt Ind AS from 1st April, 20X2 in accordance with the Companies (Indian Accounting Standard) Rules 2015.

Rahul, the senior manager, of HIM Ltd. has identified following issues which need specific attention of CFO so that opening Ind AS balance sheet as on the date of transition can be prepared:

Issue 1 : As part of Property, Plant and Equipment, Company has elected to measure land at its fair value and want to use this fair value as deemed cost on the date of transition. The carrying value of land as on the date of transition was ₹ 5,00,000. The land was acquired for a consideration of ₹ 5,00,000. However, the fair value of land as on the date of transition was ₹ 8,00,000.

Issue 2 : Under Ind AS, the Company has designated mutual funds as investments at fair value through profit or loss. The value of mutual funds as per previous GAAP was ₹ 4,00,000 (at cost). However, the fair value of mutual funds as on the date of transition was ₹ 5,00,000.

Issue 3 : Company had taken a loan from another entity. The loan carries an interest rate of 7% and it had incurred certain transaction costs while obtaining the same. It was carried at cost on its initial recognition. The principal amount is to be repaid in equal instalments over the period of loan. Interest is also payable at each year end. The fair value of loan as

© The Institute of Chartered Accountants of India

on the date of transition is ₹ 1,80,000 as against the carrying amount of loan which at present equals ₹ 2,00,000.

Issue 4 : The company has declared dividend of ₹ 30,000 for last financial year. On the date of transition, the declared dividend has already been deducted by the accountant from the company's 'Reserves & Surplus' and the dividend payable has been grouped under 'Provisions'. The dividend was only declared by board of directors at that time and it was not approved in the annual general meeting of shareholders. However, subsequently when the meeting was held it was ratified by the shareholders.

Issue 5 : The company had acquired intangible assets as trademarks amounting to ₹ 2,50,000. The company assumes to have indefinite life of these assets. The fair value of the intangible assets as on the date of transition was ₹ 3,00,000. However, the company wants to carry the intangible assets at ₹ 2,50,000 only.

Issue 6 : After consideration of possible effects as per Ind AS, the deferred tax impact is computed as ₹ 25,000. This amount will further increase the portion of deferred tax liability. There is no requirement to carry out the separate calculation of deferred tax on account of Ind AS adjustments.

Management wants to know the impact of Ind AS in the financial statements of company for its general understanding.

Prepare Ind AS Impact Analysis Report (Extract) for HIM Limited for presentation to the management wherein you are required to discuss the corresponding differences between Earlier IGAAP (AS) and Ind AS against each identified issue for preparation of transition date balance sheet. Also pass journal entry for each issue.

Answers

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

Property '1' and '2'

Para 6 of Ind AS 16 '*Property, Plant and Equipment'* defines:

"Property, plant and equipment are tangible items that:

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

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

© The Institute of Chartered Accountants of India

Paragraph 29 of Ind AS 16 states that:

"An entity shall choose either the cost model or the revaluation model as its accounting policy and shall apply that policy to an entire class of property, plant and equipment".

Further, paragraph 36 of Ind AS 16 states that:

"If an item of property, plant and equipment is revalued, the entire class of property, plant and equipment to which that asset belongs shall be revalued".

Further, paragraph 39 of Ind AS 16 states that:

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

Further, paragraph 52 of Ind AS 16 states that:

"Depreciation is recognised even if the fair value of the asset exceeds its carrying amount, as long as the asset's residual value does not exceed its carrying amount".

Property '3'

Para 6 of Ind AS 40 '*Investment property*' defines:

"Investment property is property (land or a building—or part of a building—or both) held (by the owner or by the lessee under a finance lease) to earn rentals or for capital appreciation or both, rather than for:

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

(b) sale in the ordinary course of business".

Further, paragraph 30 of Ind AS 40 states that:

"An entity shall adopt as its accounting policy the cost model to all of its investment property".

Further, paragraph 79 (e) of Ind AS 40 requires that:

"An entity shall disclose the fair value of investment property".

Further, paragraph 54 (2) of Ind AS 1 '*Presentation of Financial Statements*' requires that:

"As a minimum, the balance sheet shall include line items that present the following amounts:

(a) property, plant and equipment;

(b) investment property;

© The Institute of Chartered Accountants of India

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

(a) presented all three properties in balance sheet as 'property, plant and equipment';

(b) applied different accounting policies to Property '1' and '2';

(c) revaluation is charged in statement of profit and loss as profit; and

(d) applied revaluation model to Property '3' being classified as Investment Property.

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

Accordingly, Venus Ltd. shall apply the same accounting policy (i.e. either revaluation or cost model) to entire class of property being property '1' and '2". It also required to depreciate these properties irrespective of that, their fair value exceeds the carrying amount. The revaluation gain shall be recognised in other comprehensive income and accumulated in equity under the heading of revaluation surplus.

There is no alternative of revaluation model in respect to property '3' being classified as Investment Property and only cost model is permitted for subsequent measurement. However, Venus ltd. is required to disclose the fair value of the property in the Notes to Accounts. Also the property '3' shall be presented as separate line item as Investment Property.

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

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

Balance Sheet (extracts) as at 31st March, 20X2 ₹

Assets		
Non-Current Assets		
Property, Plant and Equipment		
Property '1'	13,500	
Property '2'	9,000	22,500
Investment Properties		
Property '3'		10,800

© The Institute of Chartered Accountants of India

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

Balance Sheet (extracts) as at 31st March, 20X2 ₹

Assets		
Non-Current Assets		
Property, Plant and Equipment		
Property '1'	16,000	
Property '2'	11,000	27,000
Investment Properties		
Property '3'		10,800
Equity and Liabilities		
Other Equity		
Revaluation Reserve		
Property '1' [16,000 – (15,000 – 1,500)]	2,500	
Property '2' [11,000 – (10,000 – 1,000)]	2,000	4,500

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

2. The above treatment needs to be examined in the light of the provisions given in Ind AS 37 'Provisions, Contingent Liabilities and Contingent Assets' and Ind AS 10 'Events After the Reporting Period'.

Para 10 of Ind AS 37 *'Provisions, Contingent Liabilities and Contingent Assets'* defines:

"Provision is a liability of uncertain timing or amount.

Liability is a present obligation of the entity arising from past events, the settlement of which is expected to result in an outflow from the entity of resources embodying economic benefits".

Further, paragraph 14 of Ind AS 37, states:

"A provision shall be recognised when:

(a) an entity has a present obligation (legal or constructive) as a result of a past event;

(b) it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation; and

© The Institute of Chartered Accountants of India

(c) a reliable estimate can be made of the amount of the obligation".

Further, paragraph 36 of Ind AS 37, states:

"The amount recognised as a provision shall be the best estimate of the expenditure required to settle the present obligation at the end of the reporting period".

Further, paragraph 3 of Ind AS 10 *'Events after the Reporting Period'* defines:

"Events after the reporting period are those events, favourable and unfavourable, that occur between the end of the reporting period and the date when the financial statements are approved by the Board of Directors in case of a company, and, by the corresponding approving authority in case of any other entity for issue. Two types of events can be identified:

(a) those that provide evidence of conditions that existed at the end of the reporting period (adjusting events after the reporting period); and

(b) those that are indicative of conditions that arose after the reporting period (non-adjusting events after the reporting period).

Further, paragraph 8 of Ind AS 10 states that:

"An entity shall adjust the amounts recognised in its financial statements to reflect adjusting events after the reporting period."

The Accountant of Sun Ltd. has not recognised the provision and accordingly not adjusted the amounts recognised in its financial statements to reflect adjusting events after the reporting period is not correct and nor in accordance with provision of Ind AS 37 and Ind AS 10.

As per given facts, the potential payment of damages to the customer is an obligation arising out of a past event which can be reliably estimated. Therefore, following the provision of Ind AS 37 '*Provisions, Contingent Liabilities and Contingent Assets'* – a provision is required. The provision should be for the best estimate of the expenditure required to settle the obligation at 31st March, 20X2 which comes to ₹ 7.5 lakhs (₹ 10 lakhs x 75%).

Further, following the principles of Ind AS 10 '*Events After the Reporting Period'* evidence of the settlement amount is an adjusting event. Therefore, the amount of provision created shall be increased to ₹ 12 lakhs and accordingly be recognised as a current liability.

3. As per given facts, the company is engaged in plantation and farming. Hence Ind AS 41 Agriculture shall be applicable to this company.

© The Institute of Chartered Accountants of India

The above facts need to be examined in the light of the provisions given in *Ind AS 20 'Accounting for Government Grants and Disclosure of Government Assistance'* and *Ind AS 41 'Agriculture'.*

Para 2(d) of Ind AS 20 *'Accounting for Government Grants and Disclosure of Government Assistance'* states:

"This Standard does not deal with government grants covered by Ind AS 41, Agriculture".

Further, paragraph 1 (c) of Ind AS 41 *'Agriculture'*, states:

"This Standard shall be applied to account for the government grants covered by paragraphs 34 and 35 when they relate to agricultural activity".

Further, paragraph 1 (c) of Ind AS 41 *'Agriculture'*, states:

"If a government grant related to a biological asset measured at its fair value less costs to sell is conditional, including when a government grant requires an entity not to engage in specified agricultural activity, an entity shall recognise the government grant in profit or loss when, and only when, the conditions attaching to the government grant are met".

Understanding of the given facts, The Company has recognised the proportionate grant for ₹ 2 lakhs in Statement of Profit and Loss before the conditions attaching to government grant are met which is not correct and nor in accordance with provision of Ind AS 41 *'Agriculture'*.

Accordingly, the accounting treatment of government grant received by the Mercury Ltd. is governed by the provision of Ind AS 41 *'Agriculture'* rather Ind AS 20 *'Accounting for Government Grants and Disclosure of Government Assistance'.*

Government grant for ₹ 10 lakhs shall be recognised in profit or loss when, and only when, the conditions attaching to the government grant are met i.e. after the expiry of specified period of five years of continuing engagement in the plantation of eucalyptus tree.

Balance Sheet extracts showing the presentation of Government Grant as on 31st March, 20X2 ₹

Liabilities	
Non-Current liabilities	
Other Non-Current Liabilities	
Government Grants	10,00,000

4. The revenue from sale of goods shall be recognised at the fair value of the consideration received or receivable. The fair value of the consideration is determined by discounting all future receipts using an imputed rate of interest where the receipt is deferred beyond normal

© The Institute of Chartered Accountants of India

credit terms. The difference between the fair value and the nominal amount of the consideration is recognised as interest revenue.

The fair value of consideration (cash price equivalent) of the sale of goods is calculated as follows: ₹

Year	Consideration (Installment)	Present value factor	Present value of consideration
Time of sale	3,33,333	-	3,33,333
End of 1st year	3,33,333	0.949	3,16,333
End of 2nd year	3,33,334	0.901	3,00,334
	10,00,000		**9,50,000**

The Company that agrees for deferring the cash inflow from sale of goods will recognise the revenue from sale of goods and finance income as follows:

Initial recognition of sale of goods		₹	₹
Cash	Dr.	3,33,333	
Trade Receivable	Dr.	6,16,667	
To Sale			9,50,000
Recognition of interest expense and receipt of second installment			
Cash	Dr.	3,33,333	
To Interest Income			33,053
To Trade Receivable			3,00,280
Recognition of interest expense and payment of final installment			
Cash	Dr.	3,33,334	
To Interest Income (Balancing figure)			16,947
To Trade Receivable			3,16,387

Statement of Profit and Loss (extracts)
for the year ended 31st March, 20X2 and 31st March, 20X3

₹

	As at 31st March, 20X2	As at 31st March, 20X3
Income		
Sale of Goods	9,50,000	-
Other Income (Finance income)	33,053	16,947

© The Institute of Chartered Accountants of India

Balance Sheet (extracts) as at 31st March, 20X2 and 31st March, 20X3

₹

	As at 31st March, 20X2	As at 31st March, 20X3
Assets		
Current Assets		
Financial Assets		
Trade Receivables	3,16,387	XXX

5. **Balance Sheet of Master Creator Private Limited as at 31st March, 20X2**

Particulars	Working/ Note reference	(₹)
ASSETS		
Non-current assets		
Property, plant and equipment	1	49,87,750
Capital work-in-progress	2	20,01,600
investment Property	3	15,48,150
Financial assets		
Other financial assets (Security deposits)		4,62,500
Other non-current assets (capital advances)	4	17,33,480
Current assets		
Inventories		5,98,050
Financial assets		
Investments (55,000 + 5,000)	5	60,000
Trade receivables	6	7,25,000
Cash and cash equivalents	7	1,16,950
Other financial assets	8	1,27,370
Other current assets (Prepaid expenses)	8	90,000
TOTAL ASSETS		**1,24,50,850**
EQUITY AND LIABILITIES		
Equity		
Equity share capital	A	10,00,000
Other equity	B	28,44,606
Non-current liabilities		
Financial liabilities		

© The Institute of Chartered Accountants of India

8% Convertible loan	11	60,60,544
Long term provisions		5,24,436
Deferred tax liability	12	2,20,700
Current liabilities		
Financial liabilities		
Trade payables	13	6,69,180
Other financial liabilities	14	1,19,299
Other current liabilities (TDS payable)	15	81,265
Current tax liabilities		9,30,820
TOTAL EQUITY AND LIABILITIES		**1,24,50,850**

Statement of changes in equity
For the year ended 31st March, 20X2

A. Equity Share Capital

	Balance (₹)
As at 31st March, 20X1	10,00,000
Changes in equity share capital during the year	-
As at 31st March, 20X2	10,00,000

B. Other Equity

	Retained Earnings (₹)	Equity component of Compound Financial Instrument (₹)	Total (₹)
As at 31st March, 20X1	21,25,975	-	21,25,975
Total comprehensive income for the year (25,00,150 + 5,000 - 85,504- 21,25,975)	2,93,671	-	2,93,671
Issue of compound financial instrument during the year	-	4,24,960	4,24,960
As at 31st March, 20X2	**24,19,646**	**4,24,960**	**28,44,606**

Disclosure forming part of Financial Statements:

Proposed dividend on equity shares is subject to the approval of the shareholders of the company at the annual general meeting and not recognized as liability as at the Balance Sheet date. (Note 9)

© The Institute of Chartered Accountants of India

Notes/ Workings: (for adjustments/ explanations)

1. Property, plant and equipment are tangible items that: (a) are held for use in the production or supply of goods or services, for rental to others, or for administrative purposes; and (b) are expected to be used during more than one period. Therefore, the items of PPE are Buildings (₹ 37,50,250) and Vehicles (₹ 12,37,500), since those assets are held for administrative purposes.
2. Property, plant and equipment which are not ready for intended use as on the date of Balance Sheet are disclosed as "Capital work-in-progress". It would be classified from PPE to Capital work-in-progress.
3. Investment property is property (land or a building—or part of a building—or both) held (by the owner or by the lessee as a right-of-use asset) to earn rentals or for capital appreciation or both, rather than for:

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

   (b) sale in the ordinary course of business.

   Therefore, Land held for capital appreciation should be classified as Investment property rather than PPE.
4. Assets for which the future economic benefit is the receipt of goods or services, rather than the right to receive cash or another financial asset, are not financial assets.
5. Current investments here are held for the purpose of trading. Hence, it is a financial asset classified as FVTPL. Any gain in its fair value will be recognised through profit or loss. Hence, ₹ 5,000 (60,000 – 55,000) increase in fair value of financial asset will be recognised in profit and loss.
6. A contractual right to receive cash or another financial asset from another entity is a financial asset. Trade receivables is a financial asset in this case and hence should be reclassified.
7. Cash is a financial asset. Hence it should be reclassified.
8. Other current financial assets:

Particulars	Amount (₹)
Interest accrued on bank deposits	57,720
Royalty receivable from dealers	69,650
Total	1,27,370

   Prepaid expenses does not result into receipt of any cash or financial asset. However, it results into future goods or services. Hence, it is not a financial asset.

© The Institute of Chartered Accountants of India

9. As per Ind AS 10, 'Events after the Reporting Period', If dividends are declared after the reporting period but before the financial statements are approved for issue, the dividends are not recognized as a liability at the end of the reporting period because no obligation exists at that time. Such dividends are disclosed in the notes in accordance with Ind AS 1, Presentation of Financial Statements.

10. 'Other Equity' cannot be shown under 'Non-current liabilities'. Accordingly, it is reclassified under 'Equity'.

11. There are both 'equity' and 'debt' features in the instrument. An obligation to pay cash i.e. interest at 8% per annum and a redemption amount will be treated as 'financial liability' while option to convert the loan into equity shares is the equity element in the instrument. Therefore, convertible loan is a compound financial instrument.

Calculation of debt and equity component and amount to be recognised in the books:

S. No	Year	Interest amount @ 8%	Discounting factor @ 10%	Amount
Year 1	20X2	5,12,000	0.91	4,65,920
Year 2	20X3	5,12,000	0.83	4,24,960
Year 3	20X4	5,12,000	0.75	3,84,000
Year 4	20X5	69,12,000	0.68	47,00,160
Amount to be recognised as a liability				59,75,040
Initial proceeds				(64,00,000)
Amount to be recognised as equity				4,24,960

* In year 4, the loan note will be redeemed; therefore, the cash outflow would be ₹ 69,12,000 (₹ 64,00,000 + ₹ 5,12,000).

Presentation in the Financial Statements:

In Statement of Profit and Loss for the year ended on 31 March 20X2

Finance cost to be recognised in the Statement of Profit and Loss (59,75,040 x 10%)	₹ 5,97,504
Less: Already charged to the Statement of Profit and Loss	(₹ 5,12,000)
Additional finance charge required to be recognised in the Statement of Profit and Loss	₹ 85,504

© The Institute of Chartered Accountants of India

In Balance Sheet as at 31 March 20X2

Equity and Liabilities	
Equity	
Other Equity (8% convertible loan)	4,24,960
Non-current liability	
Financial liability [8% convertible loan – [(59,75,040+ 5,97,504– 5,12,000)]	60,60,544

12. Since entity has the intention to set off deferred tax asset against deferred tax liability and the entity has a legally enforceable right to set off taxes, hence their balance on net basis should be shown as:

Particulars	Amount (₹)
Deferred tax liability	4,74,850
Deferred tax asset	(2,54,150)
Deferred tax liability (net)	2,20,700

13. A liability that is a contractual obligation to deliver cash or another financial asset to another entity is a financial liability. Trade payables is a financial liability in this case.

14. 'Other current financial liabilities':

Particulars	Amount (₹)
Wages payable	21,890
Salary payable	61,845
Interest accrued on trade payables	35,564
Total	1,19,299

15. Liabilities for which there is no contractual obligation to deliver cash or other financial asset to another entity, are not financial liabilities. Hence, TDS payable should be reclassified from 'Other current financial liabilities' to 'Other current liabilities' since it is not a contractual obligation.

© The Institute of Chartered Accountants of India

6. **Assessment of Preliminary Impact Assessment of Transition to Ind AS on Him Limited's Financial Statements**

Issue 1: Fair value as deemed cost for property plant and equipment:

Accounting Standards (Erstwhile IGAAP)	Ind AS	Impact on Company's financial statements
As per AS 10, Property, Plant and Equipment is recognised at cost less depreciation.	Ind AS 101 allows entity to elect to measure Property, Plant and Equipment on the transition date at its fair value or previous GAAP carrying value (book value) as deemed cost.	The company has decided to adopt fair value as deemed cost in this case. Since fair value exceeds book value, so the book value should be brought up to fair value. The resulting impact of fair valuation of land ₹ 3,00,000 should be adjusted in other equity.

Journal Entry on the date of transition

Particulars	Debit (₹)	Credit (₹)
Property Plant and Equipment Dr.	3,00,000	
To Revaluation Surplus (OCI- Other Equity)		3,00,000

Issue 2: Fair valuation of Financial Assets:

Accounting Standards (Erstwhile IGAAP)	Ind AS	Impact on Company's financial statements
As per Accounting Standard, investments are measured at lower of cost and fair value.	On transition, financial assets including investments are measured at fair values except for investments in subsidiaries, associates and JVs' which are recorded at cost.	All financial assets (other than Investment in subsidiaries, associates and JVs' which are recorded at cost) are initially recognized at fair value. The subsequent measurement of such assets are based on its categorization either Fair Value through Profit & Loss (FVTPL) or Fair Value through Other Comprehensive Income (FVTOCI) or at Amortised Cost based on business model assessment and contractual cash flow characteristics. Since investment in mutual fund are designated at FVTPL, increase of ₹ 1,00,000 in mutual funds fair value

© The Institute of Chartered Accountants of India

		would increase the value of investments with corresponding increase to Retained Earnings.

Journal Entry on the date of transition

Particulars	Debit (₹)	Credit (₹)
Investment in mutual funds Dr.	1,00,000	
To Retained earnings		1,00,000

Issue 3: Borrowings - Processing fees/transaction cost:

Accounting Standards (Erstwhile IGAAP)	Ind AS	Impact on Company's financial statements
As per AS, such expenditure is charged to Profit and loss account or capitalised as the case may be	As per Ind AS, such expenditure is amortised over the period of the loan. Ind AS 101 states that if it is impracticable for an entity to apply retrospectively the effective interest method in Ind AS 109, the fair value of the financial asset or the financial liability at the date of transition to Ind AS shall be the new gross carrying amount of that financial asset or the new amortised cost of that financial liability.	Fair value as on the date of transition is ₹ 1,80,000 as against its book value of ₹ 2,00,000. Accordingly, the difference of ₹ 20,000 is adjusted through retained earnings.

Journal Entry on the date of transition

Particulars	Debit (₹)	Credit (₹)
Borrowings / Loan payable Dr.	20,000	
To Retained earnings		20,000

Issue 4: Proposed dividend:

Accounting Standards (Erstwhile IGAAP)	Ind AS	Impact on Company's financial statements
As per AS, provision for proposed divided is made in the year when it has been	As per Ind AS, liability for proposed dividend is recognised in the	Since dividend should be deducted from retained earnings during the year when it has been declared and approved. Therefore, the provision

© The Institute of Chartered Accountants of India

declared and approved.	year in which it has been declared and approved.	declared for preceding year should be reversed (to rectify the wrong entry). Retained earnings would increase proportionately due to such adjustment

Journal Entry on the date of transition

Particulars	Debit (₹)	Credit (₹)
Provisions Dr.	30,000	
To Retained earnings		30,000

Issue 5 : Intangible assets:

Accounting Standards (Erstwhile IGAAP)	Ind AS	Impact on Company's financial statements
The useful life of an intangible asset cannot be indefinite under IGAAP principles. The Company amortised brand/trademark on a straight line basis over maximum of 10 years as per AS 26.	The useful life of an intangible asset like brand/trademark can be indefinite. Not required to be amortised and only tested for impairment. Company can avail the exemption given in Ind AS 101 as on the date of transition to use the carrying value as per previous GAAP.	Consequently, there would be no impact as on the date of transition since company intends to use the carrying amount instead of book value at the date of transition.

Issue 6: Deferred tax

Accounting Standards (Erstwhile IGAAP)	Ind AS	Impact on Company's financial statements
As per AS, deferred taxes are accounted as per income statement approach.	As per Ind AS, deferred taxes are accounted as per balance sheet approach.	On date of transition to Ind AS, deferred tax liability would be increased by ₹ 25,000.

Journal Entry on the date of transition

Particulars	Debit (₹)	Credit (₹)
Retained earnings Dr.	25,000	
To Deferred tax liability		25,000

© The Institute of Chartered Accountants of India

TEST YOUR KNOWLEDGE

Question

1. Shastra Ltd. desires to upgrade its production process since the directors believe that technology-led production is the only way the company can remain competitive. On 1 April 20X5, the company entered into a property lease arrangement in order to obtain tax benefits. However, the draft financial statements do not show a lease asset or a lease liability as on date.

   A new financial controller, CA. Sunil Raghavan, joined Shastra Ltd. before the financial year ending 31 March 20X6 and was engaged in the review of financial statements to prepare for the upcoming audit and to begin making a loan application to finance the new technology. CA. Sunil Raghavan believes that the lease arrangement should be recognized in the Balance Sheet. However, the Managing Director, Ms. Anusha Shrivastava, an MBA (Finance), strongly disagrees. She wishes to charge the lease rentals to the Statement of Profit or Loss. Her opinion is based on the understanding that the lease arrangement is merely a monthly rental payment, without any corresponding asset or obligation, since there is no 'invoice' for transfer of asset to Shastra Ltd. Her disagreement also stems from the fact that showing a lease obligation in the Financial Statements would impact the gearing ratio of the company, which could have an adverse impact on the upcoming loan application. Ms. Anusha has made it clear to CA. Sunil Raghavan that at stake is not only the loan application but also his future prospects at Shastra Ltd.

   Required:

   Discuss the potential ethical conflicts which may arise in the above scenario and the ethical principles which would guide how the financial controller should respond to the situation.

Answer

1. As per Ind AS 116, Leases, at the inception of a contract, an entity shall assess whether the contract is, or contains, a lease. A contract is, or contains, a lease if the contract conveys the right to control the use of an identified asset for a period of time in exchange for consideration.

   In accordance with the above definition, Shastra Ltd. must recognise a right-of-use asset representing the property and a corresponding lease liability for the obligation to make lease payments. At the commencement date, the right-of-use asset so recognised would include:

   - The amount of the initial measurement of lease liability;

- Any initial direct costs;
- Any costs to be incurred for dismantling or removing the underlying asset or restoring the site at the end of the lease term.

The liability for the lease obligation would be measured as the present value of future lease payments including payments that would be made towards any residual value guarantee, discounted using the rate implicit in the lease or the incremental rate of borrowing of the lessor, whichever is available.

The fact that there is no 'invoice' evidencing transfer of the asset cannot be a reason to avoid recognition of the right-of-use asset. In fact, what is being recognised is not an asset, since ownership rights are not transferred. What is sought to be recognised under Ind AS 116 is the right to use the asset in the manner required by the lessee Shastra Ltd. Further, since the lease represents an obligation to pay lease rentals in the future, a corresponding lease liability should be recognised. Not recognising the right-of-use asset or lease liability would not only be a violation of Ind AS 116, Leases, but would also be an incorrect presentation of the financial position, which is critical given that Shastra Ltd. is interested in taking a loan for its operations.

Ethical issues:

The managing director's threat to the financial controller results in an ethical dilemma for the financial controller. This pressure is greater because the financial controller is new.

Threats to fundamental principles

The fact that the position of the financial controller has been threatened if the treatment suggested by the managing director is not followed indicates that there is an **intimidation threat** to the fundamental principles of **objectivity** and **integrity**.

Further, as the manging director has flagged the risk that the company may not obtain loan financing if the lease obligation is recorded in the balance sheet, there is an **advocacy threat** because the financial controller may be compelled to follow an incorrect treatment to maximise the chances of obtaining the loan. This pressure again is greater because the financial controller is new.

Professional competence

When preparing the financial statements, the financial controller should ensure that the fundamental principle of **professional competence** should be followed, which requires that accounts should be prepared in **compliance with Ind AS**.

Thus, since the arrangement meets the Ind AS 116 criteria for a lease, the right-of-use asset and a corresponding lease liability should be recognised, as otherwise the liabilities of

© The Institute of Chartered Accountants of India

Shastra Ltd. would be understated. The ICAI Code of Ethics and Conduct sets boundaries beyond which accountants should not act. If the managing director refuses application of Ind AS 116, Leases, the financial controller should **disclose this to the appropriate internal governance authority**, and thus feel confident that his actions were ethical.

If the financial controller were to bend under pressure and **accept the managing director's proposed treatment**, this would contravene Ind AS 116 and **breach the fundamental principle of professional competence**. In such a case, he would be subject to professional misconduct under Clause 1 of Part II of Second Schedule of the Chartered Accountants Act, 1949, which states that a member of the Institute, 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 and shall not be grossly negligent in the conduct of his duties.

© The Institute of Chartered Accountants of India

TEST YOUR KNOWLEDGE

Questions

1. T Ltd is engaged in transport sector, running a fleet of buses at different routes. T Ltd has identified 3 operating segments:

- Segment 1: Local Route
- Segment 2: Inter-city Route
- Segment 3: Contract Hiring

The characteristics of each segment are as under:

Segment 1: The local transport authority awards the contract to ply the buses at different routes for passengers. These contracts are awarded following a competitive tender process; the ticket price paid by passengers are controlled by the local transport authority. T Ltd would charge the local transport authority on a per kilometer basis.

Segment 2: T Ltd operates buses from one city to another, prices are set by T Ltd on the basis of services provided (Deluxe, Luxury or Superior).

Segment 3: T Ltd also leases buses to schools under a long-term arrangement.

While Segment 1 has been showing significant decline in profitability, Segment 2 is performing well in respect of higher revenues and improved margins. The management of the company is not sure why is the segment information relevant for users when they should only be concerned about the returns from overall business. They would like to aggregate the Segment 1 and Segment 2 for reporting under 'Operating Segment'.

Required

What are the steps involved to automate the process to determine whether it is appropriate to aggregate Segments 1 and 2 with reference to Ind AS 108 'Operating Segments'?

2. New Way Ltd. decides to enter a new market that is currently experiencing economic difficulty and expects that in future the economy will improve. New Way Ltd. enters into an arrangement with a customer in the new region for networking products for promised consideration of ` 12,50,000.

At contract inception, New Way Ltd. wants to

(i) Define criteria for identifying contracts with customers, such as enforceable rights and obligations, agreement terms, and consideration.

© The Institute of Chartered Accountants of India

(ii) Establish rules to link relevant transactions to specific contracts and assign unique identifiers to each contract

Required

Advice the steps to automate the process to perform the above tasks on behalf of New Way Ltd.

Answers

1. Following steps should be followed to automate the process to determine whether it is appropriate to aggregate Segments 1 and 2 with reference to Ind AS 108 'Operating Segments':

1. Extract the relevant financial data related to Segments 1 and 2 from your accounting system.
2. Ensure that the data includes segment-specific information such as revenue, expenses, assets, liabilities, and any other relevant metrics.
3. Define the criteria for evaluating whether the segments should be aggregated.
4. Consider factors such as the nature of the business activities, economic characteristics, customer base, pricing policies, and risks and returns associated with each segment.
5. Utilize automated analysis tools or software capable of processing large volumes of financial data.
6. Apply predefined algorithms or rules to evaluate the financial performance and characteristics of Segments 1 and 2 based on the defined criteria.
7. Conduct a comparative analysis of the financial metrics and performance indicators between Segments 1 and 2.
8. Based on the analysis and findings, evaluate whether it is appropriate to aggregate Segments 1 and 2.
9. Document the rationale behind the decision, including the analysis results and supporting evidence.
10. Use tools such as business intelligence software, data visualization platforms, or custom-built reporting modules to present the aggregated and segmented data in a meaningful way.

2. A contract management system may be implemented which allows to store and organize contract documents electronically. This system can help you define and capture key contract details, such as enforceable rights and obligations, agreement terms, and consideration.

© The Institute of Chartered Accountants of India

Accordingly, the said contract management system shall be enabled to configure a mechanism to assign unique identifiers to each contract.

- Integrate the contract management system or accounting software with other operational systems, such as sales, CRM, or project management systems. This integration allows for the automatic capture and synchronization of contract-related data, ensuring that transactions associated with specific contracts are accurately linked.
- Assign specific tags or attributes to contracts based on the defined criteria, such as contract type, customer name, contract start and end dates, or specific service offerings, to enable efficient searching, filtering, and grouping of contracts based on various criteria.
- Use custom queries or predefined templates to extract information on the number of contracts identified, their characteristics, and the associated transactions. This provides visibility into the implementation of Ind AS 115 and helps to monitor compliance.

In addition to the above, the following may be adopted:

- Consider utilizing OCR technology to extract relevant information automatically. OCR can convert printed or handwritten text into machine-readable format, enabling efficient extraction of contract details for further processing and analysis.
- Apply machine learning and Neuro-Linguistic Programming (NLP) techniques to analyze and extract contract data automatically. These technologies can help identify specific contract terms, clauses, or obligations, aiding in the accurate identification and classification of contracts based on predefined criteria.
- Utilize workflow automation tools to streamline the contract identification process. Establish predefined rules or triggers within your system that automatically identify new contracts based on specific criteria and assign unique identifiers. This automation reduces manual effort and ensures consistency in contract identification.

© The Institute of Chartered Accountants of India