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CA FINAL (NEW) COURSE EXAMINATION: JANUARY 2021
ELECTIVE PAPER 6E: GLOBAL FINANCIAL REPORTING STANDARDS

*The question paper comprises **five** case study questions. The candidates are required to answer any **four** case study questions out of **five**.*

CASE STUDY 1

High Speed Limited ("the Company") is a car manufacturing company. During the year, the Company has entered into many transactions, details of which are given below. Finance controller of High Speed Limited requires your assistance in determining the accounting treatment of these transactions in accordance with Indian Accounting Standards.

1. *'High Speed Limited' manufactures and sells cars. The Company wants to foray into the two-wheeler business and therefore it acquires 30% interest in 'Quick Bikes Limited' for ₹ 5,00,000 as at 1st November, 2019 and an additional 25% stake as at 1st January, 2020 for ₹ 5,00,000 at its fair value.*

   Following is the Balance Sheet of Quick Bikes Limited as at 1st January, 2020:

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

   Quick Bikes Limited sells the motorcycles under the brand name 'Super Start' which has a fair value of ₹ 3,50,000 as at 1st January, 2020. This is a self- generated brand therefore Quick Bikes Limited has not recognized the brand in its books of accounts. Following is the separate balance sheet of the Company as at 1st January, 2020:

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

2. *While selling a car, the Company provides a written assurance to the customer that the car will function in the manner it is intended to function. However, if there is any breakdown in the car within 5 years due to manufacturing defect then the Company will replace the parts without any cost to the customer. The customer does not have the option to purchase the warranty separately. The Company has a past practice of providing routine maintenance services without any charge for 4 times over the period of 2 years from the date of purchase. Although the free maintenance services are not explicitly stated in the contract, however, the customer has a valid expectation that the Company will provide such services without any charge as advertised by the Company.*

3. *To expand further, the Company has entered into a Share Purchase Agreement ("SPA") with the shareholders of Fast Move Limited to purchase 30% stake in Fast Move Limited as at 01 June 2020 at a price of ₹ 30 per share. As per the terms of SPA, the Company has an option to purchase additional 25% stake in Fast Move Limited on or before 15th June 2020 at a price of ₹ 30 per share. Similarly, the selling shareholder has an option to sell additional 25% stake in Fast Move Limited on or before 15.06.2020 to the Company at a price of ₹ 30 per share. The decisions on relevant activities of Fast Move Limited are made in Annual General Meeting / Extraordinary General Meeting (AGM / EGM). A resolution in AGM / EGM is passed when more than 50% votes are casted in favor of the resolution. An AGM / EGM can be called by giving atleast 21 days advance notice to all shareholders.*

4. *During the year, the Company had issued Compulsory Convertible Debentures ("CCDs") on a private placement basis for ₹ 100 lakh. Each CCD is convertible into 5 shares at the end of 4 years from the date of issue and an annual interest is payable at the rate of 6% p.a. At initial recognition, the Company has recognized a liability component of compound instrument at ₹ 20,79,063. The Company also incurred expenses of ₹ 2,00,000 in connection with the issue of the instrument. Nature of expenses includes fees paid to legal advisors, registration and regulatory fees.*

5. *The Company acquired a 40% stake in New Motors Limited as at 1st October, 2020 for ₹ 8,00,000 and classified the investment in New Motors Limited as an associate. As at 1st October, 2020, the carrying amount and fair value of plant & equipment of New Motors Limited is ₹ 3,00,000 and ₹ 5,00,000 respectively with remaining useful life of 5 years (i.e. 20 quarters). From 1st October, 2020 to 31st December 2020, New Motors Limited generated a profit of ₹ 50,000.*

6. *While selling a car, the Company provides a trade discount of 1% on sale price which is mentioned on the invoice. The Company provides a credit period of 7 days to its customers however if paid upfront then the Company gives an additional cash discount of 2%. The Company also provides a voucher worth ₹ 500 with validity of 1 year which can be used at an apparel store.*

Questions:

1.1 At what amount the Company shall carry its investments in New Motors Limited in its consolidated financial statements as at 31st December 2020?

(A) ₹ 8,00,000

(B) ₹ 8,20,000

(C) ₹ 8,16,000

(D) ₹ 8,10,000 ***(2 Marks)***

1.2 How should the Company account for the trade discount, cash discount and voucher given to customers on sale of a car?

(A) Trade discount shall be reduced from the revenue however cash discount and value of voucher shall be charged as expenses.

(B) Trade discount and cash discount both shall be reduced from the revenue however value of voucher shall be charged as expenses.

(C) Trade discount, cash discount and value of voucher shall be charged as expenses.

(D) Trade discount, cash discount and value of voucher shall be reduced from revenue.

(2 Marks)

1.3 What shall be the accounting treatment of directly attributable expenses of ₹ 22 lakh incurred in connection with the issue of Compulsory Convertible Debentures?*

(A) Entire ₹ 2,00,000 shall be recognized as expenses in the statement of profit and loss in current year.

(B) Entire ₹ 2,00,000 shall be reduced from equity in current year.

(C) A proportion of ₹ 1,58,419 shall be reduced from equity and Balance of ₹ 41,581 shall be recognized as interest cost over the period of 4 years using effective interest method.

(D) Entire ₹ 2,00,000 shall be recognized as interest cost over the period of 4 years using effective interest method. ***(2 Marks)***

1.4 With more acquisitions, at the end of the year, the Company has investments in 2 subsidiaries, 3 associates and 1 joint venture. Which of the following statements is correct in relation to accounting of these investments in separate financial statements?

(A) The Company is required to measure all such investments at cost.

*** PS:** Read '₹ 22 lakh' as '₹ 2 lakh'.

(B) *The Company has an option to account the investments in associates and joint ventures using equity method of accounting and carry the investments in subsidiaries at cost.*

(C) *The Company has an option for each investment to measure either at cost or in accordance with Ind AS 109.*

(D) *The Company has an option to measure all such investments either at cost or in accordance with Ind AS 109. The option is available for each category of investments separately (i.e. subsidiaries, associates and joint venture).* ***(2 Marks)***

1.5 *What should be the accounting treatment of contingent liabilities assumed in a business combination?*

(A) *The acquirer shall recognize the contingent liabilities assumed in a business combination at its fair value if it is a present obligation that arises from the past events and its fair value can be measured reliably.*

(B) *The acquirer shall recognize the contingent liabilities assumed in a business combination at gross amount involved.*

(C) *Contingent liabilities assumed in a business combination shall not be recognized however shall be disclosed in notes to accounts.*

(D) *Contingent liabilities assumed in a business combination shall not be recognized and not be disclosed in notes to accounts.* ***(2 Marks)***

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

(i) *Pass the necessary journal entries to give effect of business combination in accordance with Ind AS 103 as at acquisition date 1^{st} January,2020. Provide working notes, Ignore deferred tax implication; and*

(ii) *Prepare a consolidated balance sheet of High Speed Limited as at 1^{st} January, 2020.* ***(7 Marks)***

1.7 *With the details provided in point 2 above, you are required to identify the performance obligations and when should the Company recognize the revenue for each of the performance obligation? How should the Company account for warranty?* ***(5 Marks)***

1.8 *With respect to the SPA entered by the Company, you are required to determine whether the Company has control over Fast Move Limited as at 1^{st} June, 2020.* ***(3 Marks)***

Answer to Case Study 1

1.1 Option (C) : ₹ 8,16,000

1.2 Option (D): Trade discount, cash discount and value of voucher shall be reduced from revenue

1.3 Option (C) : A proportion of ₹ 1,58,419 shall be reduced from equity and balance of ₹ 41,581 shall be recognised as interest cover over the period of 4 years using effective interest method

1.4 Option (D): The company has an option to measure all such investments either at cost or in accordance with Ind AS 109. The option is available for each category of investments separately (i.e. subsidiaries, associates and joint venture)

1.5 Option (A) : The acquirer shall recognise the contingent liabilities assumed in a business combination at its fair value if it is a present obligation that arises from past events and its fair value can be measured reliably.

1.6 **Note:** The question does not specify the basis of measurement of Non-controlling interest i.e. whether 'at Fair value' or 'in proportion of Net Identifiable Assets'. Therefore, the below solution is given on both the basis.

(i) **Journal Entry**

I. When NCI is measured at Fair value

		₹	₹
Plant and Equipment	Dr.	7,50,000	
Investment in bonds	Dr.	5,00,000	
Trade Receivables	Dr.	50,000	
Brand	Dr.	3,50,000	
Goodwill (balancing figure)	Dr.	5,00,000	
To Investment in Quick Bikes			10,00,000
To Profit or loss A/c (W.N.1)			1,00,000
To Trade Payables			1,50,000
To NCI (W.N.3)			9,00,000
(Being assets and liabilities acquired at fair value and previous investment considered at fair value on the acquisition date)			

II. When NCI is measured in proportion of Net Identifiable Assets'

		₹	₹
Plant and Equipment	Dr.	7,50,000	
Investment in bonds	Dr.	5,00,000	
Trade Receivables	Dr.	50,000	
Brand	Dr.	3,50,000	
Goodwill (balancing figure)	Dr.	2,75,000	
To Investment in Quick Bikes			10,00,000
To Profit or loss A/c (W.N.1)			1,00,000
To Trade Payables			1,50,000
To NCI (W.N.3)			6,75,000
(Being assets and liabilities acquired at fair value and previous investment considered at fair value on the acquisition date)			

Working Notes:

1. Calculation of fair value of shares on the acquisition date 1st January, 2020

25% Shares purchase on 1st January, 2020 (fair value)		₹ 5,00,000
30% Shares purchase on 1st November, 2019 at	₹ 5,00,000	
Fair value = [(5,00,000 / 25%) x 30%]	₹ 6,00,000	
Total consideration at fair value on acquisition date		₹ 11,00,000
Less: Cost of investment		(₹ 10,00,000)
Gain charged to Profit or Loss		₹ 1,00,000

2. Computation of Net Identifiable Assets at fair value

	₹
Plant and Equipment	7,50,000
Investment in bonds	5,00,000
Trade Receivables	50,000
Brand	3,50,000
	16,50,000
Less: Trade Payables	(1,50,000)
Net Identifiable Assets at fair value	15,00,000

3. **Measurement of Non-controlling Interest**

	By Fair Value	By Proportionate method
Share of NCI (100- 30-25)	45%	45%
Taking Fair value of shares on 1st January, 2020 as a base [(11,00,000/ 55%) x 45%]	₹ 9,00,000	
Taking Net Identifiable Assets on 1st January, 2020 as a base (15,00,000 x 45%)		₹ 6,75,000

(ii) Consolidated Balance Sheet of High Speed Limited as at 1st January, 2020

	Note No.	By Fair Value	By Proportionate method
Assets			
Non-current assets			
(a) Property, plant and equipment	1	21,00,000	21,00,000
(b) Intangible asset	2	8,50,000	6,25,000
(c) Financial assets			
(i) Investment in bonds		5,00,000	5,00,000
Current Assets			
(a) Financial assets			
(i) Trade receivables	3	1,30,000	1,30,000
(ii) Cash and cash equivalents	4	5,20,000	5,20,000
		41,00,000	38,75,000
Equity and Liabilities			
Equity			
(a) Equity share capital		5,00,000	5,00,000
(b) Other Equity	5	16,00,000	16,00,000
Non-controlling Interest		9,00,000	6,75,000
Current Liabilities			
(a) Financial liabilities			

(i) Borrowings	6	4,00,000	4,00,000
(ii) Trade Payables	7	4,50,000	4,50,000
(b) Other Current Liabilities	8	2,50,000	2,50,000
		41,00,000	38,75,000

Notes to Accounts

S. No.		₹	₹
1.	**Property, plant and equipment**		
	High Speed Ltd.	13,50,000	
	Quick Bikes Ltd.	7,50,000	21,00,000
2.	**Intangible asset (when NCI is measured at fair value)**		
	Goodwill	5,00,000	
	Brand value of Quick Bikes Ltd.	3,50,000	8,50,000
2.	**Intangible asset (when NCI is measured in proportion of NIA)**		
	Goodwill	2,75,000	
	Brand value of Quick Bikes Ltd.	3,50,000	6,25,000
3.	**Trade Receivables**		
	High Speed Ltd.	80,000	
	Quick Bikes Ltd.	50,000	1,30,000
4.	**Cash and cash equivalents**		
	Quick Bikes Ltd.		5,20,000
5.	**Other Equity - Reserves**		
	High Speed Ltd.	15,00,000	
	Add: Gain on investment of Quick Bikes Ltd.	1,00,000	16,00,000
6.	**Borrowings**		
	Short term loans of High Speed Ltd.		4,00,000
7.	**Trade Payables**		
	High Speed Ltd.	3,00,000	
	Quick Bikes Ltd.	1,50,000	4,50,000
8.	**Other Current Liabilities**		
	High Speed Ltd.		2,50,000

1.7 The car and training services are each capable of being distinct in accordance with paragraphs 27(a) and 28 of Ind AS 115, because the customer can benefit from the sale of the car on its own without the free routine maintenance services and can benefit from the routine maintenance services together with the car sold by the entity. The entity has a past practice of providing routine maintenance services without any charge for 4 times over the period of 2 years from the date of purchase.

The entity next assesses whether its promises to sell the car and to provide the routine maintenance services are separately identifiable in accordance with paragraphs 27(b) and 29 of Ind AS 115. The entity does not provide a significant service of integrating the routine maintenance services with car (see paragraph 29(a) of Ind AS 115). The routine maintenance services and car do not significantly modify or customise each other (see paragraph 29(b) of Ind AS 115). The car and the routine maintenance services are not highly interdependent or highly interrelated (see paragraph 29(c) of Ind AS 115). The entity would be able to fulfil its promise to transfer the car independently of its efforts to subsequently provide the routine maintenance services, and would be able to provide routine maintenance services to any customer that had previously acquired its car. Consequently, the entity concludes that its promise to sell the car and its promise to provide routine maintenance services are not inputs to a combined item, and, therefore, are each separately identifiable.

The car and routine maintenance services are each distinct in accordance with paragraph 27 of Ind AS 115 and therefore give rise to two separate performance obligations.

As a result, the entity allocates the transaction price to the two performance obligations (the car and the routine maintenance services) and recognises revenue when (or as) those performance obligations are satisfied.

Finally, the entity assesses the promise to provide a warranty and observes that the warranty provides the customer with the assurance that the car will function as intended for 5 years. The entity concludes, in accordance with paragraphs B28□–□B33 of Ind AS 115, that the warranty does not provide the customer with a good or service in addition to that assurance and, therefore, the entity does not account for it as a performance obligation. The entity accounts for the assurance-type warranty in accordance with the requirements in Ind AS 37.

1.8 Paragraph 10 of Ind AS 110 'Consolidated Financial Statements', states that an investor has power over an investee when the investor has existing rights that give it the current ability to direct the relevant activities, i.e. the activities that significantly affect the investee's returns.

As per the facts given in the question, High Speed Ltd. has 15 days to exercise the option to purchase 25% additional stake in Fast Move Ltd. which will give it majority voting rights of 55% (30% + 25%). This is a substantive potential voting rights which is currently exercisable.

Further, the decisions on relevant activities of Fast Move Ltd. are made in AGM / EGM. An AGM / EGM can be called by giving atleast 21 days advance notice. A resolution in AGM / EGM is passed when more than 50% votes are casted in favour of the resolution. Thus, the existing shareholders of Fast Move Ltd. are unable to change the existing policies over the relevant activities before the exercise of option by High Speed Ltd. High Speed Ltd. can exercise the option and get voting rights more than 50% at the date of AGM / EGM. Accordingly, the option contract gives High Speed Ltd. the current ability to direct the relevant activities even before the option contract is settled. Therefore, High Speed Ltd. controls Fast Move Ltd. as at 1st June, 2020.

CASE STUDY 2

Feel Fresh Limited (the Company) is into manufacturing and retailing of FMCG products listed on stock exchanges in India. The Company and its one of subsidiary has entered into various transactions accounting of which needs to be analysed in detail from the perspective of Ind AS implications. You being an Ind AS expert, CFO of the Company have appointed you to analyse the transaction based on following details:

1. *One of its products is bathing soap which the Company sells under the brand name 'Feel Fresh'. The Company does not have its own manufacturing facilities for soap and therefore it enters into arrangements with a third party to procure the soaps. The Company entered into a long term purchase contract of 10 years with M/s. Radhey. Following are the relevant terms of the contract with M/s. Radhey.*

   (i) *M/s. Radhey has to purchase a machine costing ₹ 10,00,000 from the supplier as specified by the Company. The machine will be customized to produce the soaps as designed by the Company. This machine cannot be used by M/s. Radhey to produce the soaps for buyer other than the Company due to the design specifications. The machine has a useful life of 10 years and the straight line method of depreciation is best suited considering the use of the machine.*

   (ii) *The Company will pay ₹ 4.75 per soap for the first year of contract. This is calculated based on the budgeted annual purchase of 7,00,000 soaps as follows:*

Particulars	***Per soap price***
Variable cost of manufacturing	*4.00*
Cost of machine (₹ 1,74,015 / 7,00,000 soaps)	*0.25*
M/s. Radhey's margin	*0.50*
Per soap cost to the Company	*4.75*

In case the Company purchases more than 7,00,000 (i.e. budgeted number of soaps) soaps in the first year then the cost of the machine (i.e. 0.25 per soap) will not be paid for soaps procured in excess of 7,00,000 units. However, in case Company procures less than budgeted number of soaps, then the Company will pay the differential unabsorbed cost of the machine, at the end of the year. For example, if the Company purchases only 6,00,000 soaps in first year then the differential amount of ₹ 24,015 (1,74,015 - (6,00,000 x 0.25)) will be paid by the Company to M/s. Radhey at the end of the year. Variable cost will be actualized at the end of the year.

(iii) The cost per soap will be calculated for each year in advance based on the budgeted number of soaps to be produced each year. An amount of ₹ 1,74,015 shall be considered each year for the cost of machine for year 1 to year 8 while calculating the cost per soap. Any differential under absorbed amount shall be paid by the Company to M/s. Radhey at the end of that year. A charge of ₹ 1,74,015 per annum for the machine is derived using borrowing cost of 8% p.a. For year 9 and year 10, only variable cost and margins will be paid.

(iv) M/s. Radhey does not have any right to terminate the contract but the Company has the right to terminate the contract at the end of each year. However, if the Company terminates the contract, it has to compensate M/s. Radhey for any unabsorbed cost of Machine. For example, if the Company terminates the contract at the end of second year then it has to pay ₹ 10,44,090 (i.e. 1,74,015 per year x 6 remaining years). If it terminates the contract after the 8th year then the Company does not have to pay the compensation since the cost of the machine would have been absorbed.

(v) In the first year, the Company purchases 5,50,000 soaps at ₹ 4.75 per soap.

2. To reward its employees, the Company had launched a scheme effective 1st April, 2017, in which the employees will be granted equity shares of the Company at below market price subject to certain conditions. Following details are provided:

(i) As per the scheme, each employee has an option to purchase 100 equity shares of the Company at ₹ 30 per share if the employee does not leave the Company for 3 years from the date of launch of the scheme i.e. 31st March 2020.

(ii) Once 3 years completed by an employee, he/she can exercise the option within 1 year i.e. by 31st March 2021.

(iii) The closing share price on stock exchange as at 1st April, 2017 is ₹ 62 per share with face value of ₹ 10 per share. The Company had appointed a registered valuer who derived the price of option at ₹ 50 using the Black Scholes model of option pricing.

(iv) There are a total of 300 employees eligible for the scheme. As at 31st March, 2018, 10 employees left the Company and further 14 employees are expected to leave

over the next 2 years. During the year 2018-2019, a multi-national company entered into the retail industry which is hiring experienced workforce and therefore a high attrition is observed in the retail industry. 110 employees left the Company during the year ended 31st March, 2019 and further 54 employees are expected to leave in the next one year. As at 31st March, 2020; only 160 employees are remaining with the Company out of 300.

(v) Only 150 employees exercise the option to purchase the equity share during the year ended 31st March 2021.

3. *The Company has entered into a lease agreement for its retail store as on 1st April, 2018 for a period of 10 years. A lease rental of ₹ 56,000 per annum is payable in arrears. The Company recognized a lease liability of ₹ 3,51,613 at inception using an incremental borrowing rate of 9.5% p.a. as at 1st April 2018. As per the terms of lease agreement the lease rental shall be adjusted every 2 years to give effect of inflation. Inflation cost index as notified by the Income tax department shall be used to derive the lease payments. Inflation cost index was 280 for financial year 2018-2019 and 301 for financial year 2020-2021. The current incremental borrowing rate is 8% p.a.*

4. *Vikash Retail Private Limited, a subsidiary of the Company had suffered heavy losses in previous periods. These losses are accumulated and eligible for setoff from future taxable income while calculating tax liabilities for future periods. However, there is no convincing evidence available which convey that sufficient taxable profits will be available against which tax losses can be utilized.*

5. *The Company has also launched a share based payment plan under which it will grant Stock Appreciation Rights (SAR) to the employees of its subsidiary, Vikash Retail Private Limited. As per terms of the plan, the Company (i.e. parent) will pay an amount per SAR which is the difference between current stock price of the Company and stock price of the Company after 3 years. The amount will be paid by the Company directly to those employees of the subsidiary who completes 3 years from launch of the plan.*

6. *To ensure the availability of funds at the time of settlement of the scheme, the Company purchases its own shares from the open market. The Company will sell these shares in the market after 3 years when the Company will be required to pay cash to the employees of the subsidiary.*

7. *The Company has issued share capital of ₹ 1 crore divided into 10,00,000 equity shares of ₹ 10 each. As at 1st June, 2019, the Company had issued 3,60,000 convertible warrants of ₹ 10 each. 6 warrants will be converted into 1 equity share of the Company at the end of 18 months from issue date. Warrants will not be redeemed.*

Questions:

2.1 *Which of the following statements correctly describes the accounting of lease arrangement for the retail store?*

(A) Increase in lease liability by ₹ 22,820 with corresponding debit to profit or loss.

(B) Increase in lease liability by ₹ 22,820 with corresponding increase in right of use asset.

(C) Increase in lease liability by ₹ 41,675 with corresponding debit to profit or loss.

(D) Increase in lease liability by ₹ 41,675 with corresponding increase in right of use asset. ***(2 Marks)***

2.2. What shall be the right accounting of tax losses accumulated by Vikash Retail Private Limited in its separate financial statements?

(A) The entity shall recognize the deferred tax asset on accumulated tax losses.

(B) The entity shall not recognize the deferred tax asset on accumulated tax losses neither it shall disclose in financial statements.

(C) The entity shall not recognize the deferred tax asset on accumulated tax losses however it shall disclose in financial statements the amount of accumulated tax losses and period by which it expires.

(D) The entity shall recognize the deferred tax asset on accumulated losses and shall also provide the justification in financial statements for recognition of deferred tax assets. ***(2 Marks)***

2.3 What shall be the accounting treatment of share appreciation rights given, in standalone financial statements of parent and subsidiary?

(A) Parent and subsidiary both shall account it as equity settled share based transaction with corresponding debit / credit in profit or loss.

(B) Parent shall account it as cash settled share based payment transaction with corresponding debit to investment in subsidiary. Subsidiary shall account it as equity settled share based payment transaction with corresponding credit to equity.

(C) Parent shall account it as equity settled share based payment transaction with corresponding debit to investment in subsidiary. Subsidiary shall account it as cash settled share based payment transaction with corresponding credit to equity.

(D) Parent and subsidiary both shall account it as cash settled share based transaction with corresponding debit/ credit in profit or loss. ***(2 Marks)***

2.4 Which of the following statements is correct for calculation of earnings per share of the Company for the year ended 31st March, 2020?

(A) 10,50,000 shares shall be used as denominator for calculation of both basic and diluted earnings per share.

(B) 10,00,000 shares shall be used as denominator for calculation of basic earnings per share however 10,50,000 shares shall be used as denominator for calculation of diluted earnings per share.

(C) 10,60,000 shares shall be used as denominator for calculation of both basic and diluted earnings per share.

(D) 10,00,000 shares shall be used as denominator for calculation of basic earnings per share however 10,60,000 shares shall be used as denominator for calculation of diluted earnings per share. ***(2 Marks)***

2.5 How should the Company account for the amount invested in its own shares and profit earned or loss incurred on those shares while selling back in the market (to settle the SAR scheme)?

(A) The Company shall recognize the amount invested as 'investment in equity shares' and measures it at fair value. The Company has an option to recognize the fair value gain/loss either in statement of profit and loss or in other comprehensive income.

(B) The Company shall reduce the amount invested from equity. Any gain earned or loss incurred on those shares shall also be adjusted directly in equity.

(C) Either (A) or (B) at the option of the Company.

(D) The Company shall recognize the amount invested as 'investment in equity shares'. Any gain earned or loss incurred on those shares shall be adjusted directly in equity.

(2 Marks)

2.6 Analyze the contract of the Company with M/s. Radhey and provide necessary accounting entries for first year in accordance with Ind AS with working notes. Assume all cash flows occur at the end of the year. ***(7 Marks)***

2.7 Provide necessary accounting entries during the life of share based payment scheme to account the scheme implemented by the Company. Provide working notes. ***(5 Marks)***

2.8 Calculate the deferred tax impact of the Company's investment in preference shares of Vanijya Capital Limited. Ignore education cess and surcharge, if any.* ***(3 Marks)***

Answer to Case Study 2

2.1 Option (B) : Increase in lease liability by ₹ 22,820 with corresponding increase in right of use asset

2.2 Option (C) : The entity shall not recognise the deferred tax asset on accumulated tax losses however, it shall disclose in financial statements the amount of accumulated tax losses and period by which it expires.

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* **PS:** Ignore this question.

2.3 Option (B) : Parent shall account it as cash settled share based payment transaction with corresponding debit to investment in subsidiary. Subsidiary shall account it as equity settled share based payment transaction with corresponding credit to equity.

2.4 Option (A) : 10,50,000 shares shall be used as denominator for calculation of both basic and diluted earnings per share.

2.5 Option (B) : The company shall reduced the amount invested from equity. Any gain earned or loss incurred on those shares shall also be adjusted directly in equity.

2.6 Identification of the contract (by applying para 9 of Ind AS 116)

(a) Identified asset

Feel Fresh Ltd. (a customer company) enters into a long term purchase contract with M/s Radhey (a manufacturer) to purchase a particular type and quality of soaps for 10 year period.

Since for the purpose of the contract M/s Radhey has to buy a customized machine as per the directions of Feel Fresh Ltd. and also the machine cannot be used for any other type of soap, the machine is an identified asset.

(b) Right to obtain substantially all of the economic benefits from use of the asset throughout the period of use

Since the machine cannot be used for manufacture of soap for any other buyer, Feel Fresh Ltd. will obtain substantially all the economic benefits from the use of the asset throughout the period of use.

(c) Right to direct the use

Feel Fresh Ltd. controls the use of machine and directs the terms and conditions of the contract with respect to recovery of fixed expenses related to machine.

Hence the contract contains a lease.

<u>Lease term</u>

The lease term shall be 10 years assuming reasonable certainty. Though the lessee is not contractually bound till 10th year, i.e., the lessee can refuse to make payment anytime without lessor's permission but, it is assumed that the lessee is reasonably certain that it will not exercise this option to terminate.

Identification of lease payment

Lease payments are defined as payments made by a lessee to a lessor relating to the right to use an underlying asset during the lease term, comprising the following:

(a) fixed payments (including in-substance fixed payments), **<u>less</u>** any lease incentives

(b) variable lease payments that depend on an index or a rate

(c) the exercise price of a purchase option if the lessee is reasonably certain to exercise that option

(d) payments of penalties for terminating the lease, if the lease term reflects the lessee exercising an option to terminate the lease

Here in-substance fixed payments in the given lease contract are ₹ 1,74,015 p.a. The present value of lease payment which would be recovered in 8 years @ 8% would be ₹ 10,00,000 (approx.)

Variable lease payments that do not depend on an index or rate and are not, in substance, fixed are not included as lease payments. Instead, they are recognised in profit or loss in the period in which the event that triggers the payment occurs (unless they are included in the carrying amount of another asset in accordance with other Ind AS).

Hence, lease liability will be recognized by ₹ 10,00,000 in the books of Feel Fresh Ltd. Since there are no payments made to lessor before commencement date less lease incentives received from lessor or initial direct costs incurred by lessee or estimate of costs for restoration / dismantling of underlying asset, the right of use asset is equal to lease liability.

Journal Entries

On initial recognition

ROU Asset	Dr.	10,00,000	
To Lease Liability			10,00,000
(To initially recognise the Lease Liability and the corresponding ROU Asset)			

At the end of the first year

Interest Expense	Dr.	80,000	
To Lease Liability			80,000
(To record interest expense and accrete the lease liability using the effective interest method (₹ 10,00,000 x 8%))			
Depreciation Expense (10,00,000 / 10 years)	Dr.	1,00,000	
To ROU Asset			1,00,000
(To record depreciation on ROU using the straight line method (₹ 10,00,000 / 10 years))			

Lease Liability Dr.	1,74,015	
To Bank / M/s. Radhey		1,74,015
(To record lease payment)		
Cost of soap Dr.	24,75,000	
To Bank / M/s. Radhey {5,50,000 x (4 + 0.5)}		24,75,000
(To record variable expenses paid as cost of the goods purchased)		

2.7 Journal Entries

	₹	₹
31st March, 2018		
Employee benefits expenses Dr.	4,60,000	
To Share based payment reserve (equity)		4,60,000
(Being expenses to the extent of 1/3 of expected vested equity instruments value recognized)		
Profit and Loss Account Dr.	4,60,000	
To Employee benefits expenses		4,60,000
(Being expenses transferred to Profit and Loss Account)		
31st March, 2019		
Share based payment reserve (equity) Dr.	40,000	
To Employee benefits expenses		40,000
(2/3 of expected vested equity instruments value)		
Employee benefits expenses Dr.	40,000	
To Profit and Loss Account		40,000
(Being expenses transferred to Profit and Loss Account)		
31st March, 2020		
Employee benefits expenses Dr.	3,80,000	
To Share based payment reserve (equity)		3,80,000
(Final vested equity instruments value)		
Profit and Loss Account Dr.	3,80,000	
To Employee benefits expenses		3,80,000
(Being expenses transferred to Profit and Loss Account)		

31st March, 2021			
Share based payment reserve (equity)	Dr.	8,00,000	
Bank Account (150 x 100 x 30)	Dr.	4,50,000	
To Share Capital [150 x 100 x 10]			1,50,000
To Securities Premium [150 x 100 x (50+20)]			10,50,000
To Retained Earnings (10 x 100 x 50)			50,000
(Being 150 options exercised and 10 options lapsed)			

Calculation of employee benefits expenses

Year ended 31st March	*Calculation*	*Expense for Period*	*Cumulative expense*
		₹	₹
2018	(300-10-14) employees x 100 shares x ₹ 50 x 1/3 years	4,60,000	4,60,000
2019	[{(300-10-110 -54) employees x 100 shares x ₹ 50 x 2/3 years}-4,60,000]	(40,000)	4,20,000
2020	[(160 employees x 100 shares x ₹ 50)-4,20,000]	3,80,000	8,00,000

CASE STUDY 3

A Limited and B Limited are companies registered under the Companies Act, 2013. A Limited is an Ind AS compliant entity and follows year ended March as its financial reporting period.

1. *On 1st April 2018, they entered into an agreement to jointly engage in the hospitality business. For this purpose, they formed a partnership firm with the name of M/s. Star Hotel ("the Firm"). Under the relevant laws, the partners and the Firm are not considered as separate legal entities.*

   To regulate the operations of the Firm, A Limited and B Limited entered into a partnership deed whose relevant terms and conditions are as follows:

   - *A Limited and B Limited shall be the partners of the Firm.*
   - *Consent of both partners shall be required for taking decisions on any matter which may affect the returns of the business.*
   - *The Firm shall operate a three-storied hotel as follows:*

Floor	***Rights and obligations relating to the floor***

Ground floor *(Ground floor will comprise of reception, lobby, restaurant, laundry division, and general administration office)*	*Both partners shall jointly and equally own the legal and beneficial ownership of the ground floor including all of its assets and related liabilities.* *All the costs relating to the operation of the ground floor shall be jointly and equally shared by both the partners.*
First floor *(First floor will comprise of Indian themed rooms for customers)*	*A Limited shall have legal and beneficial ownership of the first floor including all of its assets and related liabilities.* *The net profit for the period attributable to the renting of rooms of first floor shall accrue solely to the account of A Limited.*
Second floor *(Second floor will comprise of Italian themed rooms for customers)*	*B Limited shall have legal and beneficial ownership of the second floor including all of its assets and related liabilities.* *The net profit for the period attributable to the renting of rooms of second floor shall accrue solely to the account of B Limited.*
Third floor *(Third floor will comprise of a banquet hall)*	*Both the partners shall jointly and equally own legal and beneficial ownership of the third floor including all of its assets and related liabilities.* *The net profit for the period attributable to the renting of the banquet hall shall accrue equally to the account of both the partners.*

During the first year of operation of the hotel, A Limited many time doubted and objected to the manner in which the guests were preferentially convinced by the reception desk to occupy the Italian-themed rooms of the second floor.

To avoid the repetitive disputes, on 1st April 2019, A Limited and B Limited converted the partnership firm into a company named Star Hotel Private Limited ("the Company"). Under the relevant laws, the shareholders and the Company are considered as separate legal entities.

To regulate the operations of the Company, A Limited and B Limited entered into a shareholders' agreement with the following relevant terms and conditions:

- *A Limited and B Limited shall transfer their individual rights regarding the respective floors of the hotel in favour of the Company such that the Company becomes the legal and beneficial owner thereof.*

- *The Company shall assume all the liabilities of A Limited and B Limited in relation to the hotel business.*
- *In consideration of transfer of rights and obligations by A Limited and B Limited in favour of the Company, A Limited and B Limited shall receive equity shares of the Company in equal proportion.*
- *Each equity share shall entitle the holder thereof one vote in the general meetings of the Company.*
- *The Company's Board shall consist of·6 directors. All the matters in relation to the operations of the Company, except certain reserved matters, shall be decided by the Board by a vote of simple majority. In case of equality of votes in respect of any matter other than the reserved matters, the chairman shall have a casting vote.*
- *Following are the Reserved Matters in respect of which decisions shall be taken only by unanimous consent of all the directors:*
    - *(i) Approval of the operating plan for each financial year;*
    - *(ii) Capital expenditure exceeding ₹ 20 crore in a year;*
    - *(iii) Entering into borrowing arrangements for an amount which is equal to or more than 30% of the Company's net worth; and*
    - *(iv) Any matter which may affect the returns of the business.*
- *A Limited and B Limited shall have the right to nominate 3 directors each in the Board. A Limited and B Limited shall have the right to replace the directors being nominated by them respectively with any other directors of their choice. The chairman of the Board shall be nominated by A Limited.*
- *The profits of the business may be distributed by the Company to the shareholders in the form of dividends which shall be approved by a simple majority of votes in a general meeting of the Company.*
- *Shareholders shall be entitled to dividends in the proportion of the share capital held by them.*
- *Upon liquidation of the Company, its net assets, after repayment of all of its liabilities, shall be distributed to the shareholders in the proportion of share capital held by them.*
- *During the period 1st April, 2019 to 31st March, 2024, A Limited shall have the right to sell all the equity shares held in the Company to B Limited at a price which is 10% more than the fair value determined by an independent valuer. If such right is exercised by A Limited, B Limited shall be under obligation to purchase the shares in accordance with this clause.*

2. *In order to meet the cleaning needs of its hospitality business, A Limited is also engaged in the manufacturing of certain specialized chemicals. During the manufacturing process, certain wastewater is produced which is released by A Limited in the nearby river. In order to reduce pollution of the rivers, the state government has introduced a scheme with the following salient features:*

   - *If a manufacturer installs certain pre-approved wastewater treatment plant, the government will provide an interest free loan equal to 50% of the cost of the plant;*
   - *Such loan will be repayable to the government in 5 years from the date of disbursal;*
   - *The manufacturer availing the benefit of this scheme must treat the wastewater of its factory using the specified plant before releasing it to the river. If this condition is violated, the entire loan shall become immediately repayable to the government along with a penalty of ₹ 10 lakh.*

   Cost of the wastewater treatment plant to be installed to avail the benefit of the scheme is ₹ 50 lakh. A Limited decided to utilise this scheme because, if it were to obtain the similar loan from a bank, it would be available at a market interest rate of 12% per annum. Accordingly, A Limited applied for and obtained the government loan of ₹ 25 lakh on 1st April, 2018. A Limited purchased and installed the plant such that it became ready for use on the same date.

   A Limited has an accounting policy of recognising government grant in relation to depreciable assets in the proportion of depreciation expense. It has determined that the plant will be depreciated over a period of 5 years using straight-line method. In the month of March 2020, government officials conducted a surprise audit and it was found that A Limited was not using the wastewater treatment plant as prescribed. Accordingly, on 31st March, 2020, the government ordered A Limited to repay the entire loan along with penalty. A Limited repaid the loan with interest and penalty as per the order on 31st March 2020.

   Additional information:

   During the year, A Limited bought control in C Limited. A Limited paid ₹ 10,00,000 in cash and issued 5,000 shares with face value of ₹ 10 each to the shareholders of C Limited; the market value of the shares is ₹ 12.5 each. A Limited incurred issue costs of ₹ 0.5 per share. It also paid ₹ 50,000 as professional fees to carry out the above transaction.

Questions:

3.1 *What is the consideration transferred by A Limited to C Limited?*

   (A) ₹ 10,50,000

   (B) ₹ 10,62,500

   (C) ₹ 11,02,500

(D) ₹11,15,000 **(2 Marks)**

3.2 A Limited has the following options with regards to its own equity shares. Which of these should be included in the calculation of diluted earnings per share?

(A) In the money purchased put options

(B) In the money purchased call options

(C) In the money written put options

(D) Out of the money written put options ***(2 Marks)***

3.3 The following table contains different components of employee benefits cost, with four options indicating the section of the financial statements in which such component should be recognised. You are required to select the correct option.

	Option (A)	***Option (B)***	***Option (C)***	***Option (D)***
Current service cost	*Other Comprehensive Income*	*Statement of profit or loss*	*Statement of profit or loss*	*Statement of profit or loss*
Past service cost	*Other comprehensive Income*	*Statement of profit or loss*	*Other comprehensive Income*	*Other comprehensive Income*
Net interest	*Other Comprehensive Income*	*Statement of profit or loss*	*Statement of profit or loss*	*Other comprehensive Income*
Remeasurements of the net defined benefit liability	*Statement of profit or loss*	*Other comprehensive Income*	*Other comprehensive Income*	*Other Comprehensive Income*

(2 Marks)

3.4 From the following items, identify what must be classified as other long-term benefits under Ind AS 19?

(A) Paid maternity leave

(B) Cash bonus payable in August 2020 for results obtained up to 31st March, 2020

(C) Deferred compensation payable 20 months after the period in which it is earned

(D) Lump sum retirement benefit of ₹10 lakh that vests after five years of service

(2 Marks)

3.5 A Limited is considering the possibility of issuing its equity securities in the US capital market. For its regulatory filings in the USA, A Limited wants to choose US GAAP as its *reporting framework. Which income tax rate should be used for the purposes of measuring deferred tax assets and deferred tax liabilities under Ind AS and US GAAP?*

(A) Under US GAAP, enacted rates should be used; under Ind AS, enacted or substantially enacted rates should be used.

(B) Under US GAAP, enacted or substantially enacted rates should be used; under Ind AS, enacted rates should be used.

(C) Under US GAAP as well as Ind AS, enacted or substantially enacted rates should be used.

(D) Under US GAAP as well as Ind AS, enacted rates should be used. ***(2 Marks)***

3.6 How should the arrangement with B Limited be classified and recognised in the financial statements of A Limited for the year ended 31st March, 2019? Explain the basis of your conclusion. Additionally, describe the changes, if any, to the classification and recognition in the consolidated financial statements of A Limited for the year ended 31st March, 2020. ***(8 Marks)***

3.7 In respect of the wastewater plant, measure the amount of government grant as on 1st April 2018. Determine the nature of the government grant and its accounting treatment (principally) for the year ended 31st March, 2019. Also determine the impact on profit or loss if any, on account of revocation of government grant as on 31st March, 2020. ***(7 Marks)***

Answer to Case Study 3

3.1 Option (B) : ₹10,62,500

3.2 Option (C) : In the money written put options

3.3 Option (B) : Current service cost - Statement of Profit or Loss; Past service cost - Statement of Profit or Loss; Net interest - Statement of Profit or Loss; Remeasurements of the net defined benefit liability – Other Comprehensive Income.

3.4 Option (C) : Deferred compensation payable 20 months after the period in which it is earned.

3.5 Option (A) : Under US GAAP, enacted rates should be used; under Ind AS, enacted or substantially enacted rates should be used.

3.6 As per the terms and conditions of the partnership deed, consent of both the partners shall be required for taking decisions on any matter which may affect the returns of the business. Here, we can observe that both the partners have joint control over the business of the partnership firm as defined under Ind AS 111. Therefore, we can conclude that the arrangement between A Limited and B Limited is a joint arrangement under Ind AS 111.

Classification of the joint arrangement for the year ended 31st March, 2019

Next step will be to classify the joint arrangement as either joint operation or joint venture.

Para B15 of Ind AS 111 states that the classification of joint arrangements requires the parties to assess their rights and obligations arising from the arrangement. When making that assessment, an entity shall consider the following:

(a) the structure of the joint arrangement.

(b) when the joint arrangement is structured through a separate vehicle:

   (i) the legal form of the separate vehicle;

   (ii) the terms of the contractual arrangement; and

   (iii) when relevant, other facts and circumstances.

Para B24 states that the assessment of the rights and obligations conferred upon the parties by the legal form of the separate vehicle is sufficient to conclude that the arrangement is a joint operation only if the parties conduct the joint arrangement in a separate vehicle whose legal form does not confer separation between the parties and the separate vehicle (ie the assets and liabilities held in the separate vehicle are the parties' assets and liabilities).

As per para 15 of Ind AS 111, a joint operation is a joint arrangement whereby the parties that have joint control of the arrangement have rights to the assets, and obligations for the liabilities, relating to the arrangement. Those parties are called joint operators.

Accordingly, the joint arrangement is carried out through a separate vehicle M/s. Star Hotel whose legal form does not confer separation between the parties and the separate vehicle (ie the assets and liabilities held in vehicle M/s. Star Hotel are the parties' assets and liabilities ie of A Ltd. and B Ltd.). This is reinforced by the terms agreed by the parties in their contractual arrangement, which state that A Ltd. and B Ltd. have rights to the assets, and obligations for the liabilities, relating to the arrangement that is conducted through vehicle M/s. Star Hotel. [As per para B25 and B28 of Ind AS 111].

Hence, here the joint arrangement is a joint operation.

Recognition in the financial statements of A Ltd. for the year ended 31st March, 2019

A Ltd. in its financial statements for the year ended 31st March, 2019 will recognise its share of the assets and its share of any liabilities resulting from the arrangement (eg accounts payable to third parties) on the basis of its agreed participation share. It will also recognise its share of the revenue and expenses resulting from the hospitality services provided through M/s Star Hotel.

First floor that is controlled by A Limited shall be accounted for by A Limited in its financial statements.

For **the two floors (Ground Floor and Third Floor)** that are jointly controlled by A Limited and B Limited, as per the contractual arrangement, both A Limited and B Limited will jointly and equally own the legal and beneficial ownership of assets and related liabilities. Thus, A Ltd. will recognise its 50% share of the revenue and expenses resulting from these floors.

With respect to second floor, A Ltd. should not account for any items of assets and liabilities, revenue and expenses in its financial statements.

The assets, liabilities, revenue and expenses should be recognised on a line-by-line basis based on nature and classification of the respective items and according to the principles of recognition and measurement prescribed under the respective Ind AS applicable on such items.

Reclassification of the joint arrangement for the year ended 31st March, 2020

As per para B23 of Ind AS 111, the joint arrangement is carried out through a separate vehicle whose legal form causes the separate vehicle to be considered in its own right (ie the assets and liabilities held in the separate vehicle are the assets and liabilities of the separate vehicle and not the assets and liabilities of the parties).

Since the terms of the contractual arrangement in the formation of company Star Hotel Private Limited do not specify that the parties have rights to the assets, or obligations for the liabilities, relating to the arrangement. Instead, the terms of the contractual arrangement establish that the parties have rights to the net assets of Star Hotel Private Limited.

As mentioned in the case study, the legal form of the company confer separation between the shareholders and the company. Further, as per the shareholders agreement, the individual assets and liabilities of the business are legally and beneficially by the company rather than the shareholders. Upon liquidation of the company, its net assets, after repayment of all its liabilities, shall be distributed to the shareholders in the proportion of share capital held by them. It implies that the shareholders have rights to assets of the company. This is a key characteristic of a joint venture.

The terms and conditions of the shareholders' agreement do not modify or reverse the rights and obligations conferred by the legal form of the company.

Therefore, on the basis of the description of terms and conditions of the shareholders' agreement, there are no other facts and circumstances that indicate that the parties have rights to substantially all the economic benefits of the assets relating to the arrangement, and that the parties have an obligation for the liabilities relating to the arrangement.

Hence, the joint arrangement shall be reclassified from a joint operation to a joint venture in the financial statements of A Limited for the financial year ended 31st March, 2020.

Recognition in the consolidated financial statements of A Ltd. for the year ended 31st March, 2020

As per Para 24 of Ind AS 111, a joint venturer shall recognise its interest in a joint venture as an investment and shall account for that investment using the equity method in accordance with Ind AS 28 'Investments in Associates and Joint Ventures' unless the entity is exempted from applying the equity method as specified in that standard.

Accordingly, A Ltd. shall recognise its right to the net assets of Star Hotel Private Limited as investment and account for it using the equity method assuming that the right to sell the shares to B Ltd. is not substantive and will not have any implication on the assessment as it will not alter the joint arrangement.

Note: Right to sell 50% shares by A Ltd. has been ignored, since the right to exercise the option rest with A Ltd. and not B Ltd. Hence, B Ltd. is under obligation to buy but do not have potential voting rights.

3.7 As per the principles of Ind AS 20 "Accounting for Government Grants and Disclosure of Government Assistance", the benefits of a government loan at a below market rate of interest is treated as a government grant. The loan shall be recognized and measured in accordance with Ind AS 109 "Financial Instruments". The benefit of the below market rate of interest shall be measured as the difference between the initial carrying value of the loan determined in accordance with Ind AS 109 and the proceeds received. The benefit is accounted for in accordance with Ind AS 20. As per Ind AS 109, the loan should be initially measured at its fair value.

Initial recognition of grant as on 1st April 2018

Fair value of loan = ₹ 25,00,000 x 0.567 (PVF @ 12%, 5th year) = ₹ 14,17,500

A Limited will recognize ₹ 10,82,500 (25,00,000 – 14,17,500) as the government grant and will make the following entry on receipt of loan:

Date	Particulars	Dr. (₹)	Cr. (₹)
01.04.2018	Bank account Dr.	25,00,000	
	To Deferred Grant Income		10,82,500
	To Loan account		14,17,500
	(Being grant initially recorded at fair value)		

Accounting treatment for year ending 31st March, 2019

As per para 3 of Ind AS 20, grants related to assets are government grants whose primary condition is that an entity qualifying for them should purchase, construct or otherwise acquire long-term assets.

As per para 24-27 of Ind AS 20, Government grants related to assets, including non-monetary grants at fair value, shall be presented in the balance sheet either by setting up the grant as deferred income or by deducting the grant in arriving at the carrying amount of the asset.

One method recognises the grant as deferred income that is recognised in profit or loss on a systematic basis over the useful life of the asset.

The other method deducts the grant in calculating the carrying amount of the asset. The grant is recognised in profit or loss over the life of a depreciable asset as a reduced depreciation expense.

A Ltd. has adopted first method of recognising the grant as deferred income that is recognised in profit or loss on a systematic basis over the useful life of the asset. Here, deferred income is recognised in profit or loss in the proportion in which depreciation expense on the asset is recognised.

Depreciation for the year (2018-2019) = ₹ 50,00,000 / 5 years = ₹ 10,00,000

As the loan is to finance a depreciable asset, ₹ 10,82,500 will be recognized in Profit or Loss on the same basis as depreciation.

Since the depreciation is provided on straight line basis by A Limited, it will credit ₹ 2,16,500 (10,82,500 / 5) equally to its statement of profit and loss over the 5 years.

Journal Entries

Date	Particulars		Dr. (₹)	Cr. (₹)
31.03.2019	Depreciation (Profit or Loss A/c)	Dr.	10,00,000	
	To Property, Plant & Equipment			10,00,000
	(Being depreciation provided for the year)			
	Deferred grant income	Dr.	2,16,500	
	To Profit or Loss			2,16,500
	(Being deferred income adjusted)			

Impact on profit or loss due to revocation of government grant as on 31st March 2020

As per para 32 of Ind AS 20, a government grant that becomes repayable shall be accounted for as a change in accounting estimate. Repayment of a grant related to income shall be applied first against any unamortised deferred credit recognised in respect of the grant. To the extent that the repayment exceeds any such deferred credit, or when no deferred credit exists, the repayment shall be recognised immediately in profit or loss.

Amount payable to Government on account of principal loan = ₹ 25,00,000

Amount payable to Government on account of penalty = ₹ 10,00,000

Journal Entries

Date	Particulars		Dr. (₹)	Cr. (₹)
31.03.2020	Deferred grant income	Dr.	2,16,500	
	To Profit or Loss			2,16,500
	(Being deferred income adjusted)			
	Loan account (W.N.1)	Dr.	17,78,112	
	Deferred grant income (W.N.2)	Dr.	6,49,500	
	Profit or Loss	Dr.	72,388	
	To Government grant payable			25,00,000
	(Being refund of government grant)			
	Profit or Loss	Dr.	10,00,000	
	To Government grant payable			10,00,000
	(Being penalty payable to government)			

Therefore, total impact on profit or loss on account of revocation of government grant as on 31st March, 2020 will be ₹ 10,72,388 (10,00,000 + 72,388).

Circumstances giving rise to repayment of a grant related to an asset may require consideration to be given to the possible impairment of the new carrying amount of the asset.

Working Notes:

1. Amortisation Schedule of Loan

Year	Opening balance of Loan	Interest @ 12%	Closing balance of Loan
31.03.2019	14,17,500	1,70,100	15,87,600
31.03.2020	15,87,600	1,90,512	17,78,112

2. Deferred Grant Income

Year	Opening balance	Adjustment	Closing balance
31.03.2019	10,82,500	2,16,500	8,66,000
31.03.2020	8,66,000	2,16,500	6,49,500

CASE STUDY 4

1. *PQR Holdings Limited is an IFRS compliant conglomerate based in London and has Pound sterling ("GBP") as its functional and presentation currency. On 1st April, 2019, PQR Holdings Limited incorporated PQR India Limited as its wholly owned subsidiary in India. PQR India will be engaged in trading of items purchased from PQR Holdings. The shares of PQR India, having a face value of ₹ 10 each amounting to total of ₹ 500 crore, were issued to PQR Holdings in GBP on 1st April, 2019.*

   PQR India has adopted Ind AS with effect from its incorporation. In accordance with Ind AS, management of PQR India has concluded that its functional currency is Indian Rupee ("INR"). Following is the summarized trial balance of PQR India as on 31st March, 2020, being the reporting date of PQR India and PQR Holdings:

   *(**Note**: All amounts in the below mentioned trial balance are ₹ in crore)*

S. No.	***Particulars***	***Debit Balances***	***Credit Balances***
1.	*Share capital*	-	*500.0*
2.	*Securities premium reserve on issue of equity shares*	-	*150.0*
3.	*Retained earnings*	-	*110.0*
4.	*Long-term borrowings*	-	*30.0*
5.	*Deferred tax liability*	-	*10.0*
6.	*Income tax payable*	-	*25.0*
7.	*Import duty payable*	-	*5.0*
8.	*Employee benefits payable*		*7.5*
9.	*Sundry trade payables*	-	*2.5*
10.	*Property, plant and equipment (net of depreciation)*	*550.0*	-
11.	*Computer software (net of amortisation)*	*70.0*	-
12.	*Inventories purchased on 15th March, 2018** *(there is no indicator of impairment)*	*200.0*	
13.	*Cash and bank balance*	*5.0*	-

* **PS:** Read '15th March, 2018' as '15th March, 2020'.

14.	*Sundry trade receivables*	*17.0*	*-*
15.	*Allowance for doubtful trade receivables*	*-*	*2.0*
	Total	*842.0*	*842.0*

Additional information relating to property, plant and equipment, and computer software:

Line item	***Date of acquisition***
Property, plant and equipment	*30th April, 2019*
Computer software	*5th May, 2019*

Accounting policy of PQR India in relation to shareholders' funds:

Since IFRS does not provide guidance on how to translate equity (that is, share capital and reserves), PQR India has adopted the following accounting policy:

Share capital	*To be translated using historical exchange rate*
Securities premium	*To be translated using historical exchange rate*
Retained earnings	*To be translated using average exchange rate*

Since the presentation currency of PQR Holdings is GBP, PQR India is required to translate its trial balance from INR to GBP. Following table provides relevant foreign exchange rates:

Closing spot rate as on 1st April, 2019	*1 INR = 0.0123 GBP*
Closing spot rate as on 30th April, 2019	*1 INR = 0.0120 GBP*
Closing spot rate as on 5th May, 2019	*1 INR = 0.0119 GBP*
Closing spot rate on 15th March, 2020	*1 INR = 0.0108 GBP*
Closing spot rate as on 31st March, 2020	*1 INR = 0.0109 GBP*
Average exchange rate for the year ended 31st March, 2020	*1 INR = 0.0116 GBP*

2. *On 1st June 2019, VK Ltd determines that it has a highly probable forecasted purchase of plant and machinery costing USD 1,00,000 from AZ Inc, a US-based company. The purchase will take place on 30th April, 2020. VK Ltd has Indian Rupee as its functional currency, and AZ Inc has US dollar as its functional currency. On 1 June 2019, VK Ltd. enters into a forward contract to purchase US $ 60,000 to partially meet the forecast US dollar payment. The forward contract locks in the value of the US dollar amount at a rate of US $ 1 = INR 74; the relevant information is as follows:*

Date	***USD-INR Spot rate***	***USD-INR Forward rate***	***Fair value of Forward (INR)***

1st June, 2019	*72*	*74*	*0*
30th June, 2019	*73*	*73.5*	*1,50,000*
30th September, 2019	*75*	*75.5*	*1,80,000*
31st December, 2019	*77*	*76.5*	*1,50,000*
31st March, 2020	*76*	*75.5*	*1,20,000*
30th April, 2020	*75*	*74*	*60,000*

***Note**: The fair value of the forward contract is provided by the banking counterparty. Any discounting impact may be ignored.*

Other information:

3. *SS Limited has recognized goodwill worth ₹ 40,00,000 in the past for a business combination. During the current year, it has impaired the goodwill by ₹ 8,00,000 and therefore the carrying amount of goodwill is ₹ 32,00,000. Amortisation or impairment of goodwill is not deductible as per the tax regulations applicable in the jurisdiction where SS Limited files its tax returns. Applicable tax rate is 30%.*

4. *During the financial year ended 31st March, 2020, an entity (TM limited) decided to sell one of its manufacturing divisions. All the criteria indicating that the sale is highly probable were met during the financial year ending 31st March, 2020, except for the marketing, which began only on 10th April, 2020.*

Questions:

4.1 *What is the amount of deferred tax to be recognised by SS Limited on goodwill?*

(A) Deferred tax liability of ₹ 9,60,000

(B) Deferred tax liability of ₹ 12,00,000

(C) Deferred tax asset of ₹ 12,00,000

(D) No deferred tax ***(2 Marks)***

4.2 *TM Limited is preparing its financial statements for the year ending 31st March, 2020 and requires your guidance on the disclosures with respect to the sale of the manufacturing division. Accordingly, choose the incorrect statement from the following options:*

(A) Adjust the financial statements for the effect of discontinued operations

(B) Include a description of the manufacturing division in the notes

(C) Include the reportable segment in which the manufacturing division is presented as per Ind AS 108 'Operating Segments' (if applicable) in the notes.

(D) Describe the facts and circumstances leading to the expected disposal and the expected manner and timing of that disposal in the notes. ***(2 Marks)***

4.3 *TM Limited enters into a number of transactions each year. The accountant has requested your help to identify which of these must be accounted for as a business combination :*

(A) TM Limited purchases 30% equity in TP Ltd, an unlisted company.

(B) TM Limited purchases a 45% interest which gives it control over TR Ltd.

(C) TM Limited purchases one of many brand names and products of TQ Ltd.

(D) TM Limited purchases a 30% equity and invests in debentures of TS Ltd. ***(2 Marks)***

4.4 *Which of the following are typical features of a service concession arrangement? (select one or more)*

(A) The contract sets the initial prices to be levied by the operator.

(B) Any price revisions over the period of the service contract are at the discretion of the operator.

(C) The operator has to hand over the infrastructure to the grantor at the end of the arrangement.

(D) The operator is not responsible for any management of the infrastructure or related services and therefore acts as an agent of the grantor. ***(2 Marks)***

4.5 *Which of the following categories of financial assets is NOT subject to impairment requirements of Ind AS 109 "Financial Instruments"?*

(A) Equity instruments measured at fair value through profit or loss.

(B) Investment in debentures where (i) Contractual cash flows represent solely payment of principal and interest; and (ii) entity's business model is to hold financial assets in order to collect contractual cash flows.

(C) Lease receivables

(D) Trade debtors ***(2 Marks)***

4.6 *As the accountant of PQR India, you are required to do the following for its separate financial statements:*

(a) Explain the principle of monetary and non-monetary items. Based on this principle, bifurcate the line items of the trial balance into monetary and non-monetary items. ***(3 Marks)***

(b) Translate the trial balance of PQR India from INR to GBP. ***(4 Marks)***

4.7 *The Finance Manager of VK Ltd is wondering if it is necessary to follow hedge accounting under Ind AS, given that the whole transaction will be completed in less than a year. As the accountant at VK Ltd, you are required to do the following:*

(a) What are the benefits of designating the forward contract into a hedging relationship, as compared to not making such a designation? ***(3 Marks)***

(b) Assume that the hedge is designated on 1st June, 2019, and the purchase transaction of plant and machinery occurred on 30th April, 2020 as expected. Assume that the hedge is perfectly matched and effective, and no hedge ineffectiveness actually occurred at each testing date.

Prepare the journal entries (along with necessary explanations) to be passed as at each of the relevant dates as mentioned above in the table. ***(5 Marks)***

Answer to Case Study 4

4.1 Option (D) : No deferred tax

4.2 Option (A) : Adjust the financial statements for the effect of discontinued operations.

4.3 Option (B) : TM Limited purchases a 45% interest which gives it control over TR Ltd.

4.4 Option (A) : The contract sets the initial prices to be levied by the operator &

Option (C) : The operator has to hand over the infrastructure to the grantor at the end of the arrangement.

4.5 Option (A) : Equity instruments measured at fair value through profit or loss

4.6 **(a)** Monetary items are units of currency held and assets and liabilities to be received or paid in a fixed or determinable number of units of currency. Para 15 of Ind AS 21 states that the essential feature of a monetary item is a right to receive (or an obligation to deliver) a fixed or determinable number of units of currency. Similarly, a contract to receive (or deliver) a variable number of the entity's own equity instruments or a variable amount of assets in which the fair value to be received (or delivered) equals a fixed or determinable number of units of currency is a monetary item.

Conversely, the essential feature of a non-monetary item is the absence of a right to receive (or an obligation to deliver) a fixed or determinable number of units of currency.

On the basis of above principles, the line items of trial balance should be bifurcated as follows:

Particulars	Monetary item / Non-monetary item
Share Capital	Non-monetary item
Securities Premium reserve on issue of equity shares	Non-monetary item

Retained earnings	Non-monetary item
Long-term borrowings	Monetary item
Deferred tax liability	Non-monetary item
Income tax payable	Monetary item
Import duty payable	Monetary item
Employee benefits payable	Monetary item
Sundry trade payables	Monetary item
Property, plant and equipment (net of depreciation)	Non-monetary item
Computer software (net of amortization)	Non-monetary item
Inventories purchased (there is no indicator of impairment)	Non-monetary item
Cash and bank balance	Monetary item
Sundry trade receivables	Monetary item
Allowance for doubtful trade receivables	Monetary item

As per para 38 of Ind AS 21, an entity may present its financial statements in any currency (or currencies). If the presentation currency differs from the entity's functional currency, it translates its results and financial position into the presentation currency. For example, when a group contains individual entities with different functional currencies, the results and financial position of each entity are expressed in a common currency so that consolidated financial statements may be presented.

(b) Translation of the balances for the purpose of consolidation

Particulars	INR in crore	Rate (GBP)	Amount in GBP
Property, plant and equipment (net of depreciation)	550.0	0.0109	5.995
Computer software (net of amortization)	70.0	0.0109	0.763
Inventories	200.0	0.0109	2.18
Cash and bank balance	5.0	0.0109	0.0545
Sundry trade receivables net of allowance for doubtful trade receivables (17.0-2.0)	15.0	0.0109	0.1635
Total Assets	840.0		9.156
Share Capital	500.0	0.0123	6.15
Securities Premium reserve	150.0	0.0123	1.845

Retained earnings	110.0	0.0116	1.276
Long-term borrowings	30.0	0.0109	0.327
Deferred tax liability	10.0	0.0109	0.109
Income tax payable	25.0	0.0109	0.2725
Import duty payable	5.0	0.0109	0.0545
Employee benefits payable	7.5	0.0109	0.08175
Sundry trade payables	2.5	0.0109	0.02725
Foreign Currency Translation reserve recognised in OCI (balancing figure)	____		(0.987)
Total Equity and liabilities	840.0		9.156

Note: The above table of conversion may also be shown in the form of trial balance.

4.7 (a) Benefits of designating the forward contract into a hedge relationship, as compared to not making such a designation

VK Ltd. has a highly probable forecast purchase of plant and machinery costing USD 1,00,000 from AZ Inc. expected to take place on 30th April, 2020. On 1st June, 2019, VK Ltd. enters into a forward contract to purchase US$ 60,000 to partially meet the forecast US dollar payment.

Hedge accounting is beneficial even though the transaction will be completed in less than one year and the forward contract covers only 60% of the forecast transaction amount of USD 1,00,000.

- If hedge accounting were not applied, the gain/loss on the hedging instrument would be recognised in a profit and loss in each reporting period, resulting in some volatility in profit and loss.

- However, if hedge accounting is applied, and if no significant sources of ineffectiveness have been identified, the gain / loss on forward contract would be accumulated in the cash flow hedge reserve rather than in profit or loss. Upon purchase of plant and machinery, the amount that has been accumulated in the cash flow hedge reserve would be removed from it and will be included directly in the initial cost of the plant and machinery (Para 6.5.11(d)(i) of Ind AS 109). In other words, the initial carrying amount of the asset will be equivalent to recognising the purchase translated at the contracted rate for the hedged portion and the spot rate on capitalisation for the unhedged portion. This would result in reduction of volatility in profit or loss.

(b) **Journal Entries**

Date	Particulars	Dr. (₹)	Cr. (₹)
1.6.2019	No entry as initial fair value is zero	-	-
30.6.2019	Forward contract Dr. To Cash flow hedge reserve - Effective change in fair value through OCI (Being effective part of change in fair value of the instrument recognised in OCI)	1,50,000	 1,50,000
30.9.2019	Forward contract Dr. To Cash flow hedge reserve-Effective change in fair value through OCI (Being effective part of change in fair value of the instrument recognised in OCI)	30,000	 30,000
31.12.2019	Cash flow hedge reserve - Effective change in fair value through OCI Dr. To Forward contract (Being effective part of change in fair value of the instrument recognised in OCI)	30,000	 30,000
31.3.2020	Cash flow hedge reserve - Effective change in fair value through OCI Dr. To Forward contract (Being effective part of change in fair value of the instrument recognised in OCI)	30,000	 30,000
30.4.2020	Cash flow hedge reserve -Effective change in fair value through OCI Dr. To Forward contract (Being effective part of change in fair value of the instrument recognised in OCI)	60,000	 60,000
30.4.2020	Bank / Cash Dr. To Forward Contract (Being effective part of change in fair value of the instrument recognised in OCI)	60,000	 60,000

30.4.2020	Property, Plant and Equipment Dr. Cash flow hedge reserve - Effective change in fair value through OCI Dr. To Creditors/ Bank (Being machinery purchased at USD 1,00,000 recognised at spot rate of ₹ 75 per USD)	74,40,000 60,000	 75,00,000

CASE STUDY 5

1. *NM Limited is an Ind AS compliant multinational company which is engaged in various businesses. CD Limited, a subsidiary of NM Limited, also follows Ind AS for its financial reporting and is engaged in the business of consultation for civil engineering projects such as highways, buildings, etc. On 1st April 2019, CD Limited won a contract to provide consultancy to the government in relation to a highway project. Following are the salient features of the contract:*

   - *Total period for which CD Limited is required to provide consultancy is 2 years starting from 1st April 2019.*
   - *Total consultancy fees to be received by CD Limited during the contract period is ₹ 50 crore.*
   - *On 1st April 2019, NM Limited will be required to provide a performance guarantee to the government for an amount up to ₹ 50 crore. If the consultancy services provided by CD Limited is not satisfactory, the government can invoke the performance guarantee. If the guarantee is invoked, NM Limited will be required to indemnify the government for the loss suffered because of non-satisfactory performance by CD Limited.*

   To execute the project, on 1st April 2019, CD Limited has availed a short- term loan of ₹ 30 crore from the bank with the following covenants:

   - *NM Limited shall provide a financial guarantee for an amount up to ₹ 30 crore.*
   - *If CD Limited makes any default on repayment of the loan, NM Limited will be required to indemnify the bank up to an amount of ₹ 30 crore.*

   For providing the above-mentioned two guarantees, NM Limited has charged commission from CD Limited at the market rate of 1% of the guaranteed amount applicable to such guarantees. As per the revenue recognition policy of NM Limited, it has decided to recognise the guarantee commission income in profit or loss over a period of two years starting from 1st April 2019 using the straight-line method.

   Based on the performance and credit history of CD Limited, the management of NM Limited has established that there is no need to recognise any impairment allowance.

The CFO of NM Limited is of the opinion that both the guarantees given should not be recognised in the balance sheet of NM Limited. However, she believes that these guarantees should be disclosed as contingent liabilities in the notes to the financial statements.

2. *Following is the summarised statement of profit and loss of NM Limited as per Ind AS for the year ended 31st March 2020:*

Particulars	**₹ in crore**
Revenue from operations	*580.00*
Other income	*28.00*
(A) Total income	***608.00***
Purchases of stock-in-trade	*20.00*
Changes in inventories of stock-in-trade	*3.00*
Employee benefits expense	*58.00*
Finance costs	*65.00*
Depreciation and amortization expense	*15.00*
Other expenses	*150.00*
(B) Total expenses	***311.00***
(C) Profit before tax	***297.00***
Current tax	*82.70*
Deferred tax	*0.75*
(D) Tax expense	***83.45***
(E) Profit after tax [C-D]	***213.55***

Additional information:

- *Corporate income tax rate applicable to NM Limited in India is 30%.*
- *Other income includes long-term capital gains of ₹ 5 crore which are taxable at the rate of 10%.*
- *Other expenses include the following items which are not deductible for income tax purposes:*

Item	**₹ in crore**
Penalties	*0.50*
Impairment of goodwill	*22.00*
Corporate Social Responsibility expense	*3.00*

- *Other expenses include research and development (R & D) expenditure of ₹ 4 crore in respect of which a 200% weighted deduction is available under income tax laws.*

- *Other income includes dividends of ₹ 2 crore, which is exempt from tax.*
- *Profit before tax of ₹ 297 crore includes (i) agriculture income of ₹ 25 crore which is exempt from tax; and (ii) profit of ₹ 30 crore earned in the USA on which NM Limited has paid tax at the rate of 20%.*
- *Depreciation as per income tax laws is ₹ 12.5 crore.*

During review of the financial statements of NM Limited, the CFO multiplied profit after tax by the Indian income tax rate and arrived at ₹ 89.10 crore as the tax expense (₹ 297 crore x 30% = ₹ 89.10 crore). However, actual income tax expense appearing in the summarized statement of profit and loss is ₹ 83.45 crore.

Other information:

3. *NM Limited's subsidiary P Limited is engaged in the business of jewellery. P Limited is planning to introduce a scheme named "Buy Now, Pay Later" for its slow moving inventory. Under the scheme, the customer can buy jewellery and pay the amount due after a period of one year from the invoice date. The credit period can be increased or decreased depending on the customer's requirements; the pricing in such cases will be appropriately adjusted in accordance with the prevalent market rates. Management is of the view that the scheme will boost its sales significantly, as the customers will not have to avail loans from financial institutions to purchase the jewellery, whose prevailing market interest rate is 12% per annum. Management of P Limited expects that all of its customers who avail the benefit of the scheme will pay the amount on their respective due dates without any default.*
4. *S Limited is a subsidiary of H Limited. S Limited's functional and presentation currency is INR, while the functional currency of its parent is USD and its presentation currency is EUR. S Limited has a firm commitment to buy a commodity in EUR. It has entered into a forward contract to hedge the firm commitment against foreign exchange risk. It has to prepare its financial statements for the purpose of consolidation financial statement for its parent.*
5. *Q Limited is a huge machine manufacturer. It has to overhaul its machinery every 3 years. It has purchased machinery worth ₹ 50,00,000. It is estimated that the overhaul costs will be ₹ 5,00,000. It is expected that the machine has a useful life of 10 years.*

Questions:

5.1 *The CFO of P Limited is preparing for an upcoming presentation explaining the impact of the "Buy Now, Pay Later" scheme, and the differences between Companies (Accounting Standards) Rules, 2006 ("IGAAP") as compared with Ind AS. Which of the following statements accurately summarises the accounting treatment?*

(A) *Under IGAAP, the revenue was recognised at its fair value determined by discounting the invoiced amount using 12% per annum as the discounting rate;*

however, under Ind AS, revenue will be recognised at the amount invoiced to the customer.

(B) Under IGAAP, the revenue was recognised at the amount invoiced to the customer; the same accounting treatment will continue under Ind AS.

(C) Under IGAAP, the revenue was recognised at the amount invoiced to the customer; however, under Ind AS, revenue recognition will be deferred until the expiry of the credit period.

(D) Under IGAAP, the revenue was recognised at the amount invoiced to the customer; however, under Ind AS, revenue will be recognised at its fair value to be determined by discounting the invoiced amount using 12% per annum as the discounting rate.

(2 Marks)

5.2 How can S Limited account for a hedge relationship for the purpose of preparing H Limited's consolidated financial statements?

(A) Cash flow hedge

(B) Fair value hedge

(C) Option to designate under cash flow hedge or fair value hedge

(D) Net investment hedge

5.3 How should Q Limited initially recognise the purchase of its machinery? ***(2 Marks)***

(A) Recognise the machine at its cost of ₹ 50,00,000 and depreciate over 10 years.

(B) Recognise two assets - the machine worth ₹ 45,00,000 to be depreciated over 10 years and costs related to overhaul of ₹ 5,00,000 to be depreciated over 3 years.

(C) Recognise two assets - the machine worth ₹ 50,00,000 to be depreciated over 10 years and costs related to overhaul of ₹ 5,00,000 to be depreciated over 3 years.

(D) Recognise an asset for ₹ 45,00,000 to be depreciated over 10 years and expense ₹ 5,00,000 immediately. ***(2 Marks)***

5.4 A company prepares segment information for its management reporting purposes. Under Ind AS 108 'Operating Segments', the company can also use this segment information to determine the appropriate segments for financial reporting. Applying this approach, which of these are the company's reportable segments under Ind AS 108?

(A) Segments deemed significant by the management and are reviewed regularly by them

(B) Segment whose information is presented by the company's industry peers

(C) Each segment whose operating results are reviewed regularly by the Board of directors of the company to make decisions about resources to be allocated to the segment

(D) Each segment whose operating results are reviewed regularly by the Managing director who is the chief operating decision maker to make decisions about resources to be allocated to the segment. ***(2 Marks)***

5.5 Which of the following is incorrect in respect of a cash flow statement under Ind AS?

(A) The cash flow effects of disposals cannot be deducted from those of acquisitions.

(B) Cash payment to the shareholders for buying back its shares is a financing activity.

(C) An entity only includes the transactions between itself and the joint venture when preparing the consolidated cash flow statement.

(D) Non-cash investing and financing transactions are to be disclosed as part of the cash flow statement. ***(2 Marks)***

5.6 (A) Comment on the accounting and disclosure principles proposed by the CFO in respect of each of the guarantees. ***(2 Marks)***

(B) Provide necessary journal entries, if any, as on 1st April, 2019, and 31st March, 2020 in the books of NM Limited. ***(6 Marks)***

5.7 The CFO has sought your help in reconciling the difference between the two tax expense amounts. Prepare a reconciliation containing the disclosures as required under the relevant Ind AS. ***(7 Marks)***

Answer to Case Study 5

5.1 Option (D) : Under IGAAP, the revenue was recognized at the amount invoiced to the customer; however, under Ind AS, revenue will be recognized at its fair value to be determined by discounting the invoiced amount using 12% per annum as the discounting rate.

5.2 Option (C) : Option to designate under cash flow hedge or fair value hedge.

5.3 Option (B) : Recognize two assets – the machine worth ₹ 45,00,000 to be depreciated over 10 years and costs related to overhaul of ₹ 5,00,000 to be depreciated over 3 years.

5.4 Option (D) : Each segment whose operating results are reviewed regularly by the Managing director who is the chief operating decision maker to make decisions about resources to be allocated to the segment.

5.5 Option (D) : Non-cash investing and financing transactions are to be disclosed as part of the cash flow statement.

5.6 (A) Accounting and Disclosure of Performance guarantee and Financial guarantee:

1. Performance Guarantee

Performance guarantee relates to satisfactory performance of the subsidiary to the Government for the consultancy on highway project. Since CD Ltd. has good performance and credit history, CFO of NM Ltd. correctly opine that there is no need to recognise such guarantee as liability in the books of NM Ltd. However, the entity may apply Ind AS 37 to determine whether it meets the criteria to be disclosed as a contingent liability in its financial statements. Hence, in this case the view of CFO is correct.

2. Financial Guarantee

Since financial guarantee is in relation to a debt instrument (it is in relation to the loan taken by CD Limited), it fulfills the definition of a financial guarantee. Accordingly, NM Limited shall apply Ind AS 109 to recognize and measure the financial guarantee in its financial statements. Therefore the views expressed by CFO is not in line with Ind AS.

A financial guarantee contract is initially recognised at fair value. If the guarantee is issued on a commercial basis, the initial fair value is likely to equal the premium received.

Subsequently, at the end of the reporting period, financial guarantee will be measured at the higher of:

- The amount of the loss allowance, and
- The amount initially recognised less cumulative amortisation, where appropriate.

As the loss allowance is expected to be zero and the guarantee being for not more than 12 months, NM Ltd. shall derecognise the guarantee liability of ₹ 0.30 crore and recognise guarantee commission income of ₹ 0.30 crore.

The contention of CFO is wrong because paragraph 2 of Ind AS 37, ‘Provisions, Contingent Liabilities and Contingent Assets’, states that it does not apply to financial instruments (including guarantees) that are within the scope of Ind AS 109, ‘Financial Instruments’. Therefore, disclosure of financial guarantees as contingent liabilities is neither in accordance with Ind AS 109 nor in accordance with Ind AS 37.

(B) Journal Entries in the books of NM Limited:

(i) With respect to performance guarantee

<u>1st April 2019</u>

Cash/Bank A/c (50 crore x 1%)	Dr.	0.50 crore	
To Deferred Commission income			0.50 crore
(Receipt of commission)			

<u>31st March 2020</u>

Deferred Commission income (0.50 crore/2 years)	Dr.	0.25 crore	
To Profit and Loss			0.25 crore

(Commission income recognise in Profit and loss over the two year period on SLM)

(ii) With respect to financial guarantee

<u>Initial Measurement (1st April 2019):</u>

Investment in CD Ltd. (Subsidiary)/(Cash/bank)	Dr.	0.30 crore	
To Financial guarantee liability			0.30 crore
(Being guarantee initially recorded)			

<u>Subsequent Measurement (31st March 2020):</u>

Subsequent recognition of commission income <u>as it is a short term loan</u>

Financial guarantee liability	Dr.	0.30 crore	
To Commission income			0.30 crore

(Being guarantee liability subsequently reversed on completion and commission income recognised)

5.7 Reconciliation of income tax expense and current tax as per accounting profit for the year ended 31st March, 2020

Particulars		₹ in crore
Accounting profit		<u>297.00</u>
Tax at the applicable tax rate of 30%		89.10
Tax effect of expenses that are not deductible in determining taxable profits:		

Penalties (0.50 x 30%)	0.15	
Impairment of goodwill (22.00 x 30%)	6.60	
Corporate social responsibility expense (3.00 x 30%)	0.90	7.65
Tax effect of expenses that are deductible in determining taxable profits:		
Research and development expenses (4.00 x 30%)		(1.20)
Tax effect of income that are exempted in determining taxable profits:		
Dividend income (Exempt) (2.00 x 30%)	0.60	
Agriculture income (Exempt) (25.00 x 30%)	7.50	(8.10)
Tax effect of income on which different tax rates are used for determining taxable profits:		
Differential income tax on long term capital gain (5.00 x 20%)	1.00	
Foreign income in USA (30.00 x 10%)	3.00	(4.00)
Income tax expense (Current) reported in the Statement of Profit and Loss for the current year		83.45

Reconciliation of deferred tax:

Particulars	₹ in crore
Deferred tax in relation to Property, plant and equipment and intangible assets [(15-12.5) x 30%]	0.75
Tax expense (deferred) reported in the Statement of Profit and Loss for the current year	0.75