

DISCLAIMER

This Suggested Answer hosted on the website do not constitute the basis for evaluation of the student's answers in the examination. The answers are prepared by the Faculty of the Board of Studies with a view to assist the students in their education. Alternate Answers have been incorporated, wherever necessary. While due care is taken in preparation of the answers, if any error or omission is noticed, the same may be brought to the attention of the Director of Board of Studies. The Council of the Institute is not in anyway responsible for the correctness or otherwise of the answers published herein.

Further, in the Elective Papers which are Case Study based, the solutions have been worked out on the basis of certain assumptions/views derived from the facts given in the question or language used in the question. It may be possible to work out the solution to the case studies in a different manner based on the assumptions made or views taken.

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

LT Ltd. is a multinational company engaged in the manufacture of chemicals. JK Ltd., a wholly owned subsidiary of LT Ltd., is a public utility entity engaged in distribution of electricity within a certain geographical area to the general public. LT Ltd. has a manufacturing plant within the same geographical area and therefore purchases electricity from JK Ltd. The rates / tariffs are as fixed by the regulatory authority for generation and distribution of electricity.

LT Ltd. acquired 60% of the equity shares of KR Ltd. on 1st April, 2021 when KR Ltd. retained earnings were ₹ 4,00,000. During the year ended 31st March, 2022, KR Ltd. purchased goods from LT Ltd. for ₹ 2,00,000. At 31st March, 2022, half of these goods were still in the inventory of KR Ltd. LT Ltd. applies a mark-up of 25% on cost to all of its sales. At 31st March, 2022, the retained earnings of LT Ltd. and KR Ltd. were ₹ 7,50,000 and ₹ 5,40,000 respectively.

LT Ltd. is in the process of constructing a building. The construction process is expected to take about 18 months from 1st January, 2020 to 30th June, 2021. The building meets the definition of a qualifying asset. LT Ltd. incurs the following expenditure for the construction:

1 st January, 2020	₹ 5 crores
30 th June, 2020	₹ 20 crores
31 st March, 2021	₹ 20 crores
30 th June, 2021	₹ 5 crores

On 1st July, 2020, LT Ltd. issued 10% Redeemable Debentures of ₹ 50 crores. The proceeds from the debentures form part of the company's general borrowings, which it uses to finance the construction of the qualifying asset, ie, the building. LT Ltd. had no borrowings (general or specific) before 1st July, 2020 and did not incur any borrowing costs before that date. LT Ltd. incurred ₹ 25 crores of construction costs before obtaining general borrowings on 1st July, 2020 (pre-borrowing expenditure) and ₹ 25 crores after obtaining the general borrowings (post-borrowing expenditure).

LT Ltd.'s customer has filed a legal claim for damages to the extent of ₹ 15 lakhs. There is an 80% probability that the decision will not be in favour of LT Ltd. and it will have to pay for the damages claimed. However, there is a 10% chance that LT Ltd. will win the case and a 10% probability that an out-of-court settlement is reached. In both of these scenarios, no cost is expected to be incurred.

LT Ltd. is planning to dispose off a collection of assets costing ₹ 2.5 crores. LT Ltd. designates these assets as a disposal group. The carrying amount of these assets immediately before classification as held for sale was ₹ 2 crores. Upon being classified as held for sale, the assets were revalued to ₹ 1.8 crores. Estimates indicate that it would cost ₹ 10 lakhs to sell these assets

On 1st January 2022, LT Ltd. acquired a 60% stake in DR Ltd. The cash consideration was ₹ 10 lakhs payable immediately and ₹ 12.1 lakhs payable after two years. The fair value of net assets of DR Ltd. at acquisition date was ₹ 30 lakhs. LT Ltd. calculated its cost of capital to be 10%. Non-controlling interest is measured at the proportion of identifiable net assets.

LT Ltd. sold a group of machinery with a written down value of ₹ 40 lakhs to SLB Ltd. for ₹ 50 lakhs and the same set of machinery was leased back as an operating lease by SLB Ltd. to LT Ltd.

Multiple Choice Questions:

1.1 Considering the transactions with KR Ltd., what would be the adjusted retained earnings in LT Ltd.'s consolidated statement of financial position as at 31st March, 2022?

(A) ₹ 12,40,000

- (B) ₹ 8,54,000
(C) ₹ 8,14,000
(D) ₹ 8,00,000
- 1.2 With respect to the legal claim for damages filed by its customer, what provision should LT Ltd. recognize in its books of account?
- (A) ₹ 15 lakhs
(B) ₹ 9 lakhs
(C) ₹ 6 lakhs
(D) Nil
- 1.3 Which ONE of the following is not a related party of LT Ltd.?
- (A) AR Ltd., where Mrs. R (wife of Mr. R) has significant influence and Mr. R has joint control over LT Ltd.
(B) XY Ltd., whose Director Mr. Y having significant influence over XY Ltd., is also a Director of LT Ltd.
(C) A Ltd. a subsidiary of LT Ltd.
(D) Son of Managing Director of LT Ltd.
- 1.4 What would be the carrying amount of the disposal group in the entity's accounts after its classification as held for sale?
- (A) ₹ 2.4 crores
(B) ₹ 1.9 crores
(C) ₹ 1.7 crores
(D) ₹ 1.8 crores
- 1.5 Calculate the amount of goodwill / gain on bargain purchase by DR Limited arising upon acquisition of DR Ltd.
- (A) Gain on bargain purchase ₹ 10 lakhs
(B) Gain on bargain purchase ₹ 8 lakhs
(C) Goodwill ₹ 2.1 lakhs
(D) Goodwill ₹ 2 lakhs
- (5 x 2 Marks each = 10 Marks)**

Descriptive Questions

- 1.6 Discuss whether the transactions between LT Ltd. and JK Ltd. should be disclosed as per requirements of IAS 24 Related Party Disclosures, in the financial statements of JK Ltd.
- (4 Marks)**

1.7 In respect of the sale and leaseback of machinery with SLB Ltd., analyse the accounting treatment in the books of LT Ltd. for each of the following scenarios:

Scenario 1-- Fair value is ₹ 50 lakhs and Sale price is ₹ 50 lakhs

Scenario 2-- Fair value is ₹ 60 lakhs and Sale price is ₹ 50 lakhs

Scenario 3 --Fair value is ₹ 45 lakhs and Sale price is ₹ 38 lakhs

Scenario 4 --Fair value is ₹ 40 lakhs and Sale price is ₹ 50 lakhs

Scenario 5 --Fair value is ₹ 46 lakhs and Sale price is ₹ 50 lakhs

Scenario 6 --Fair value is ₹ 35 lakhs and Sale price is ₹ 39 lakhs **(6 Marks)**

1.8 For each of the financial years ended 31st March 2020, 2021 and 2022, calculate the borrowing cost that LT Ltd. is permitted to capitalize as a part of the building cost.

(5 Marks)

ANSWER TO CASE STUDY 1

1.1 Option (C) : ₹ 8,14,000

1.2 Option (A) : ₹ 15 lakhs

1.3 Option (B) : XY Ltd. whose Director Mr. Y having significant influence over XY Ltd. is also a Director of LT Ltd.

1.4 Option (C) : ₹ 1.7 crores

1.5 Option (D) : Goodwill ₹ 2 lakh

1.6 As per paragraph 9(b)(i) of IAS 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, JK Ltd is a related party of LT Ltd from the perspective of financial statements of LT Ltd.

Paragraph 11 of IAS 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, JK Ltd is a public utility. Had the only relationship between JK Ltd and LT Ltd been that of a supplier and a consumer of electricity, JK Ltd would not have been regarded as a related party of LT Ltd. However, as per the facts of the given case, this is not the only relationship between LT Ltd and JK Ltd. Apart from being a customer or buyer of electricity from JK Ltd., LT Ltd is also a parent company of JK Ltd. This is a relationship that is covered within the related party relationships to which the disclosure requirements of the standard apply. In view of the above, the buying of electricity from JK Ltd. by LT 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 LT Ltd is charged the electricity tariffs determined by an independent rate-setting authority (i.e., the terms of supply to LT Ltd. are at par with those applicable to other consumers)

IAS 24 does not exempt an entity from disclosing related party transactions merely because they have been carried out on an arm's length basis.

- 1.7 This part of the question has been taken from IAS 17. However, IAS 17 has been repealed by IFRS 16. As per IFRS 16 following information are required for accounting of sale and lease back transaction:

1. Whether the transfer is sale or not?
2. Whether the seller-lessee have a 'substantive repurchase option' for the underlying asset (i.e., a right to repurchase the asset).
3. Annual lease payments
4. Interest rate implicit in the lease
5. Lease term

Though assumptions may be possible for 1 and 2 above, the information referred to in 3, 4 and 5 above are necessarily required for computation. Since the above information are not available in the case study, a solution under IFRS 16 cannot be prepared.

- 1.8 Applying paragraph 17 of IAS 23 to the fact pattern, the entity would not begin capitalising borrowing costs until it incurs borrowing costs (i.e. from 1st July, 2020)

In determining the expenditures on a qualifying asset to which an entity applies the capitalisation rate (paragraph 14 of IAS 23), the entity does not disregard expenditures on the qualifying asset incurred before the entity obtains the general borrowings. Once the entity incurs borrowing costs and therefore satisfies all three conditions in paragraph 17 of IAS 23, it then applies paragraph 14 of IAS 23 to determine the expenditures on the qualifying asset to which it applies the capitalisation rate.

Calculation of borrowing cost for financial year 2019-2020

Expenditure		Capitalization Period (current year)	Weighted average Accumulated Expenditure
Date	Amount		
1 st January, 2020	₹ 5 crore	0/3	Nil

Borrowing Costs eligible for capitalisation = NIL. LT Ltd. cannot capitalise borrowing costs before 1st July, 2020 (the day it starts to incur borrowing costs).

Calculation of borrowing cost for financial YEAR 2020-2021

Expenditure		Capitalization Period (current year)	Weighted average Accumulated Expenditure
Date	Amount		
1 st January, 2020	₹ 5 crore	9/12	₹ 3.75 crore
30 th June, 2020	₹ 20 crore	9/12	₹ 15 crore
31 st March, 2021	₹ 20 crore	0/12	Nil
Total			₹ 18.75 crore

Borrowing Costs eligible for capitalisation = 18.75 cr. x 10% = ₹ 1.875 cr. LT Ltd. cannot capitalise borrowing costs before 1st July, 2020 (the day it starts to incur borrowing costs). Accordingly, this calculation uses a capitalization period from 1st July, 2020 to 31st March, 2021 for this expenditure.

Calculation of borrowing cost for financial year 2021-2022

Expenditure		Capitalization Period (current year)	Weighted average Accumulated Expenditure
Date	Amount		
1 st January, 2020	₹ 5 crore	3/12	₹ 1.25 crore
30 th June, 2020	₹ 20 crore	3/12	₹ 5 crore
31 st March, 2021	₹ 20 crore	3/12	₹ 5 crore
31 st March, 2021	₹ 1.875 crore	3/12	₹ 0.47 crore

30 June 2021	₹ 5 crore	0/12	Nil
Total			₹ 11.72 crore

Borrowing Costs eligible for capitalisation = ₹ 11.72 cr. x 10% = ₹ 1.172 cr.

Case Study: 2

On 1st January, 2022, Globe Ltd. enters into a contract with Ruby Ltd. to provide asset management services for five years. The entity receives a management fee of two per cent per annum based on the client's assets under management at the end of each quarter. At 31st March, 2022, Ruby Ltd.'s assets under management are ₹ 100 crores. In addition, Globe Ltd. receives a performance-based incentive fee of 20 per cent of the fund's return in excess of the return of an observable market index over the five-year period. Consequently, both the management fee and the performance fee in the contract are variable consideration.

Globe Ltd. issues ₹ 1 crore convertible bonds, on 1st July 2021. The bonds have a life of eight years and a face value of ₹ 10 each, and they offer interest, payable at the end of each financial year, at a rate of 6 per cent per annum. The bonds are issued at their face value and each bond can be converted into one ordinary share in Globe Ltd. at any time in the next eight years. Companies of a similar risk profile have recently issued debt with similar terms, without the option for conversion, at a rate of 8 per cent per annum.

On 1st April, 2021, Globe Ltd. incurred ₹ 2,000 selling costs to sell a good to Grey Ltd. for ₹ 95,000. In general, Globe Ltd. does not extend any credit to its customers. However, as a special case, the sale agreement with Grey Ltd. provided that the customer would pay ₹ 95,000 selling price in full, on 31st March, 2022. The prevailing rate for one-year credit granted to trade customers in the industry is 10% per year. This is the clearly determinable way of determining the imputed rate of interest.

On 1st July, 2021, Globe Ltd. sold a new computer system for ₹ 4,00,000, which also included after sales support for a period of 2 years from the date of supply of the computer system. Globe Ltd. estimates the cost of the after-sales support at ₹ 60,000 and the fair value of such after-sales support is estimated to be ₹ 90,000.

On 31st March, 2019, Globe Ltd. acquired 30 per cent of the ordinary shares that carry voting rights of Earth Ltd. for 1,00,000. In acquiring those shares Globe Ltd. incurred transaction costs of ₹ 1,000. At 31st March 2020, 2021 and 2022, for impairment of assets, management assessed the fair values of its investment in Earth Ltd. as ₹ 1,02,000, ₹ 1,10,000 and ₹ 90,000 respectively. Costs to sell are estimated at ₹ 4,000 throughout.

Globe Ltd. acquired 30% of the voting shares of AB Ltd. on 1st April, 2017. The purchase consideration was ₹ 20 crores, and Globe Ltd. has significant influence over AB Ltd. The retained earnings of AB Ltd. were ₹ 5 crores at the date of acquisition. The retained earnings of AB Ltd. at 31st March, 2022 were ₹ 10 crores.

Globe Ltd. has contracted to purchase a specialized item of machinery from an overseas supplier for USD 48 million on the following terms:

Non-refundable payment on signing of contract (1 st January, 2022)	60%
Payment on delivery and installation (5 th April, 2022)	40%
The following exchange rates are relevant:	₹ to USD
1 st January, 2022	78
31 st March, 2022	77
5 th April, 2022	79

Multiple Choice Questions:

- 2.1 What is the revenue to be recognised by Globe Ltd. for the sale of good to Grey Ltd.?
- (A) ₹ 95,000
 (B) ₹ 86,364
 (C) ₹ 85,500
 (D) ₹ 93,000
- 2.2 How much revenue should Globe Ltd. recognize from the sale of new computer system for the financial year ended 31st March, 2022?
- (A) ₹ 3,10,000
 (B) ₹ 4,00,000
 (C) ₹ 3,55,000
 (D) ₹ 3,40,000
- 2.3 Globe Ltd. measures its investment in Earth Ltd. as on 31st March 2020, 2021 and 2022 respectively at:
- (A) ₹ 1,00,000, ₹ 1,00,000, ₹ 1,00,000
 (B) ₹ 1,01,000, ₹ 1,01,000, ₹ 90,000
 (C) ₹ 98,000, ₹ 1,06,000, ₹ 86,000
 (D) ₹ 98,000, ₹ 1,01,000, ₹ 86,000
- 2.4 Calculate the carrying value of the investment in AB Ltd. in the group financial statements at 31st March, 2022.

- (A) ₹ 20 crores
 (B) ₹ 35 crores
 (C) ₹ 21.50 crores
 (D) ₹ 25 crores
- 2.5 What is the exchange loss/gain to be recognized as on 31st March, 2022 on account of the USD deposit paid for specialized item of machinery from the overseas supplier?
- (A) ₹ 4.8 crores exchange gain
 (B) ₹ 2.88 crores exchange gain
 (C) ₹ 2.88 crores exchange loss
 (D) No exchange gain or loss is to be recognised **(5 x 2 Marks each = 10 Marks)**

Descriptive Questions

- 2.6 Analyse the revenue to be recognised for the year ended 31st March, 2022 in relation to the contract with Ruby Ltd. **(5 Marks)**
- 2.7 (i) Prepare the accounting entries for initial recognition of convertible bonds.
 (ii) Calculate the interest expense across the eight years of the life of the bonds
 (iii) Prepare the accounting entries assuming that the holders of the bonds elect to convert the bonds to ordinary shares at the end of the third year (after receiving their interest payments) **(4 +3+ 3 = 10 Marks)**

Answer to Case Study 2

- 2.1 **Either Option (B) : ₹ 86,364** (If one does not opt for practical expedient in determining the transaction price)
Alternatively Option (A) : ₹ 95,000 (If one opts for practical expedient in determining the transaction price)
- 2.2 **Option (A) : ₹ 3,10,000**
- 2.3 **Option (D) : ₹ 98,000, ₹ 1,01,000, ₹ 86,000**
- 2.4 **Option (C) : ₹ 21.5 crores**
- 2.5 **Option (D) : No exchange gain or loss is to be recognised**
- 2.6 Globe Ltd. accounts for the services as a single performance obligation because it is providing a series of distinct services that are substantially the same and have the same pattern of transfer (the services transfer to the customer over time and use the same method to measure progress, that is, a time-based measure of progress).

Globe Ltd. observes that the promised consideration is dependent on the market and thus is highly susceptible to factors outside its influence. In addition, the incentive fee has a large number and a broad range of possible consideration amounts. The entity also observes that its experience is of little predictive value in determining the future performance of the market. Therefore, at contract inception, Globe Ltd. cannot conclude that it is highly probable that a significant reversal in the cumulative amount of revenue recognised would not occur if the entity includes its estimate of the management fee or the incentive fee in the transaction price.

At each reporting date, Globe Ltd. updates its estimate of the transaction price. Consequently, at the end of each quarter, Globe Ltd. concludes that it can include in the transaction price the actual amount of the quarterly management fee because the uncertainty is resolved. However, Globe Ltd. concludes that it cannot include its estimate of the incentive fee in the transaction price at those dates. This is because there has not been a change in its assessment from contract inception — the variability of the fee based on the market index indicates that the entity cannot conclude that it is highly probable that a significant reversal in the cumulative amount of revenue recognised would not occur if the entity includes its estimate of the incentive fee in the transaction price.

At 31st March, 2022, Ruby Ltd.'s assets under management are ₹ 100 crore. Therefore, the resulting quarterly management fee and the transaction price is ₹ 50 lakhs (₹ 100 crore x 2% x 3/12).

At the end of each quarter, Globe Ltd. allocates the quarterly management fee to the distinct services provided during the quarter. This is because the fee relates specifically to Globe Ltd.'s efforts to transfer the services for that quarter, which are distinct from the services provided in other quarters.

Consequently, Globe Ltd. recognises ₹ 50 lakhs as revenue for the quarter ended 31st March 2022.

2.7 (i) Computation of equity and liability component of convertible bond at 8% market rate

	₹
Present value of principal to be received at the end of 8 th year discounted at 8% (1,00,00,000 x 0.540)	54,00,000
Annuity of annual interest discounted at 8% for 8 years (1,00,00,000 x 6% x 5.747)	<u>34,48,200</u>
Total present value (a)	88,48,200
Equity component (balancing figure) (a-b)	<u>11,51,800</u>
Total proceeds received from issuance of convertible bonds (b)	<u>1,00,00,000</u>

Journal Entries

	Dr. (₹)	Cr. (₹)
On initial recognition i.e. 1 st July, 2021		
Bank A/c Dr.	1,00,00,000	
To Convertible bonds A/c (liability)		88,48,200
To Convertible bonds A/c (equity)		11,51,800
(Being recognition of convertible bonds at the date of issuance into liability and equity components)		

(ii) Table showing computation of interest expense at 8% market rate and actual interest outflow @ 6%

Date	Opening bond liability	Actual interest outflow @ 6%	Interest expense @ 8%	Increase in liability	Closing bond liability
a	b	c = 1 cr x 6% x a	d = b x 8% x a	e = d - c	f = b + e
1 st July, 2021	88,48,200				88,48,200
31 st March, 2022	88,48,200	4,50,000	5,30,892	80,892	89,29,092
31 st March, 2023	89,29,092	6,00,000	7,14,327	1,14,327	90,43,419
31 st March, 2024	90,43,419	6,00,000	7,23,474	1,23,474	91,66,893
31 st March, 2025	91,66,893	6,00,000	7,33,351	1,33,351	93,00,244
31 st March, 2026	93,00,244	6,00,000	7,44,020	1,44,020	94,44,264
31 st March, 2027	94,44,264	6,00,000	7,55,541	1,55,541	95,99,805
31 st March, 2028	95,99,805	6,00,000	7,67,984	1,67,984	97,67,789
31 st March, 2029	97,67,789	6,00,000	7,81,423	1,81,423	99,49,212
30 th June, 2029	99,49,212	1,50,000	2,00,788*	50,788	1,00,00,000

*difference of ₹ 1,804 (2,00,788 – 1,98,984) is due to rounding off

(iii) When holders of the bonds elect to convert the bonds to ordinary shares at the end of third year of bond (after receiving their interest payments), the entries would be:

	Dr. (₹)	Cr. (₹)
30th June, 2024		
Interest expense A/c (91,66,893 x 8% x 3/12) Dr.	1,83,338	

To Convertible bonds A/c (liability)		33,338
To Bank A/c		1,50,000
(Being interest expense for 3 months recorded at market rate of 8% and actual interest paid @ 6%)		
Convertible bonds A/c (liability) (91,66,893 + 33,338)	Dr.	92,00,231
Convertible bonds A/c (equity)	Dr.	11,51,800
To Ordinary share capital A/c		1,03,52,031
(Being bonds converted into ordinary shares of Globe Ltd.)		

Note:

Since these are debt instruments and it is always implied that the interest is to be paid before conversion, interest payable by Globe Ltd. for 3 months i.e. for the period 1st April, 2024 to 30th June, 2024 has been considered in the above journal entry.

However, alternatively it may be ignored on the ground that question mentioned that interest is payable at the end of the each financial year, then the entries at the time of conversion of bonds would be as follows:

		Dr. (₹)	Cr. (₹)
30th June, 2024			
Convertible bonds A/c (liability)	Dr.	91,66,893	
Convertible bonds A/c (equity)	Dr.	11,51,800	
To Ordinary share capital A/c			1,03,18,693
(Being bonds converted into ordinary shares of Globe Ltd.)			

Alternative Solution**Note:**

The above solution was given on the assumption that the bonds are optionally convertible i.e. in case the holder does not avail the option to convert the bonds into ordinary shares by the 8th year, the bonds will be redeemed.

However, alternatively it may be assumed that the bonds are mandatorily convertible i.e. in case the holder does not avail the option to convert the bonds into ordinary shares by the 8th year, the bonds will be mandatorily converted into shares. In such a situation the financial liability will equal to the present value of the amount of interest paid on the bond and rest of the bond's proceeds will be equity component. Accordingly, in such a case, the answer will be as follows:

(i) **Computation of equity and liability component of convertible bond at 8% market rate**

	₹
Annuity of annual interest discounted at 8% for 8 years (1,00,00,000 x 6% x 5.747)	<u>34,48,200</u>
Total present value (a)	34,48,200
Equity component (balancing figure) (a-b)	<u>65,51,800</u>
Total proceeds received from issuance of convertible bonds (b)	<u>1,00,00,000</u>

Journal Entries

	Dr. (₹)	Cr. (₹)
1st July, 2021		
Bank A/c Dr.	1,00,00,000	
To Convertible bonds A/c (liability)		34,48,200
To Convertible bonds A/c (equity)		65,51,800
(Being recognition of convertible bonds at the date of issuance into liability and equity components)		

(ii) **Table showing computation of interest expense at 8% market rate and actual interest outflow @ 6%**

Date	Opening bond liability	Actual interest outflow @ 6%	Interest expense @ 8%	Decrease in liability	Closing bond liability
a	b	c = 1 cr x 6% x a	d = b x 8% x a	e = d - c	f = b + e
1 st July, 2021	34,48,200				34,48,200
31 st March, 2022	34,48,200	4,50,000	2,06,892	2,43,108	32,05,092
31 st March, 2023	32,05,092	6,00,000	2,56,407	3,43,593	28,61,499
31 st March, 2024	28,61,499	6,00,000	2,28,920	3,71,080	24,90,419
31 st March, 2025	24,90,419	6,00,000	1,99,234	4,00,766	20,89,653

31 st March, 2026	20,89,653	6,00,000	1,67,172	4,32,828	16,56,825
31 st March, 2027	16,56,825	6,00,000	1,32,546	4,67,454	11,89,371
31 st March, 2028	11,89,371	6,00,000	95,150	5,04,850	6,84,521
31 st March, 2029	6,84,521	6,00,000	54,762	5,45,238	1,39,283
30 th June, 2029	1,39,283	1,50,000	10,717	1,39,283	-

* difference of ₹ 426 (11,143 – 10,717) is due to rounding off

- (iii) When holders of the bonds elect to convert the bonds to ordinary shares at the end of third year of bond (after receiving their interest payments), the entries would be:

	Dr. (₹)	Cr. (₹)
30th June, 2024		
Interest expense A/c (24,90,419 x 8% x 3/12) Dr.	49,808	
Convertible bonds A/c (liability) Dr.	1,00,192	
To Bank A/c		1,50,000
(Being interest expense for 3 months recorded at market rate of 8% and actual interest paid @ 6%)		
Convertible bonds A/c (liability) (24,90,419 - 1,00,192) Dr.	23,90,227	
Convertible bonds A/c (equity) Dr.	65,51,800	
To Ordinary share capital A/c		89,42,027
(Being bonds converted into ordinary shares of Globe Ltd.)		

Note:

Since these are debt instruments and it is always implied that the interest is to be paid before conversion, interest payable by Globe Ltd. for 3 months i.e. for the period 1st April, 2024 to 30th June, 2024 has been considered in the above journal entry.

However, alternatively it may be ignored on the ground that question mentioned that interest is payable at the end of the each financial, then the entries at the time of conversion of bonds would be as follows:

		Dr. (₹)	Cr. (₹)
30th June, 2024			
Convertible bonds A/c (liability)	Dr.	24,90,419	
Convertible bonds A/c (equity)	Dr.	65,51,800	
To Ordinary share capital A/c			90,42,219
(Being bonds converted into ordinary shares of Globe Ltd.)			

Case Study: 3

On 1st April, 2021, Bruce Ltd. began joint construction of a pipeline with another investor. Bruce Ltd. and the other investor have signed a contract that provides for joint operation and ownership of the pipeline. All of the ongoing expenditure, comprising maintenance plus borrowing costs, are shared equally. The pipeline was completed and ready for use on 1st October 2021, at which date its estimated useful life was 20 years.

The pipeline was first used on 1st January, 2022. The total cash cost of constructing the pipeline was ₹ 8 crores. This cost was partly financed by a loan of ₹ 2 crores taken out on 1st April, 2021. The loan carries interest at an annual rate of 10% with interest payable in arrears on 31st March each year. Between 1st January, 2022 and 31st March, 2022, it was necessary to spend ₹ 8,00,000 on maintenance costs.

On 1st April, 2021, Bruce Ltd. purchased some land for ₹ 2 crores (including legal costs of ₹ 20 lakhs) in order to construct a new factory that would produce electric vehicles. Construction work commenced on 1st May, 2021. Bruce Ltd. incurred the following costs in connection with its construction:

- Preparation and leveling of the land- ₹ 6,00,000.
- Purchase of materials for the construction- ₹ 1,21,60,000 in total.
- The following costs were incurred during the construction period:
 - Employment of construction workers - ₹ 4,00,000 per month.
 - Overhead costs incurred directly on the construction of the factory - ₹ 2,00,000 per month.
 - Ongoing overhead costs allocated to the construction project using Bruce Ltd.'s normal overhead allocation model - ₹ 1,00,000 per month.
- Income received during the temporary use of the factory premises as a car park during the construction period- ₹ 1,00,000.

The factory was completed on 30th November, 2021 (which is considered as substantial period of time) and production began on 1st February, 2022. The overall useful life of the factory building was estimated at 40 years from the date of completion. However, it is estimated that the roof will need to be replaced 20 years after the date of completion and that the cost of replacing the roof at current prices would be 30% of the total cost of the building.

At the end of the 40-year period, Bruce Ltd. has a legally enforceable obligation to demolish the factory and restore the site to its original condition. The directors estimate that the cost of demolition at the end of 40 years' time (based on prices prevailing at that time) will be ₹4 crores. An annual risk adjusted discount rate which is appropriate to this project is 8%. The present value of ₹1 payable in 40 years' time at an annual discount rate of 8% is 4.6 paise,

The construction of the factory was partly financed by a loan of ₹ 3.5 crores taken out on 1st April, 2021. The loan was at an annual rate of interest of 6%. During the period 1st April, 2021 to 31st August, 2021 (when the loan proceeds had been fully utilized to finance the construction) Bruce Ltd. received investment income of ₹ 2,00,000 on the temporary investment of the proceeds.

On 1st April, 2021, Bruce Ltd. raised loan finance from European investors. The investors subscribed for € 100 million (61 Loan Note) at par. Bruce Ltd. incurred incremental issue costs of € 2 million. Interest of € 8 million is payable annually on 31st March, starting on 31st March, 2022. The loan is repayable in € after 10 years on 31st March, 2031 at a premium and the effective interest rate implicit in the loan is 10% per annum. The appropriate measurement basis for this loan is amortized cost.

Relevant exchange rates are as follows:

- 1st April, 2021 - € 1 = ₹ 82
- 31st March, 2022 – € 1 = ₹ 85
- Average for year ended 31st March, 2022 – € 1 = ₹ 83

Bruce Ltd. has a subsidiary, Gulf Ltd. Gulf Ltd. has borrowed ₹ 10 crores through an inter-
corporate deposit from Bruce Ltd. for one year at an interest rate of 8% without any processing charges. Market rate of interest is 11% with an additional 1% towards processing charges.

On 1st April, 2020, Bruce Ltd. granted share options to 200 senior executives. The options will vest on 31st March, 2023 subject to the following conditions:

- Each executive will be entitled to 2,000 options if the cumulative profit in the three-year period from 1st April, 2020 to 31st March, 2023 exceeds ₹6 crores. If the cumulative profit for this period is between ₹ 7 crores and ₹ 8 crores, then 3,000 options will vest. If the cumulative profit for the period exceeds ₹ 8 crores, then 4,000 options will vest.

- If an executive leaves during the three-year vesting period, then management would forfeit any rights of share options to those executives.
- Notwithstanding the above, no options will vest unless the share price at 31st March, 2023 exceeds ₹5.

Details of the fair value of the shares and share options at relevant dates are as follows:

Date	Fair Value of Bruce Ltd.'s each share	Fair value of Bruce Ltd.'s each option
1 st April, 2020	₹ 4.00	₹ 0.50
31 st March, 2021	₹ 4.40	₹ 0.60
31 st March, 2022	₹ 4.60	₹ 0.75

The estimate of the cumulative profit for the three-year period ending 31st March, 2023 was revised each year as follows:

Date	Expected profit for the three -year period
1 st April, 2020	₹ 6.4 crores
31 st March, 2021	₹ 7.8 crores
31 March 2022	₹ 9 crores

On 1st April, 2020, none of the relevant executives were expected to leave in the three-year period from 1st April, 2020 to 31st March, 2023 and none left in the year ended 31st March, 2021. However, 10 executives left unexpectedly on 31st December, 2021. None of the other executives are expected to leave before 31st March, 2023. Bruce Ltd. correctly reflected this arrangement in its financial statements for the year ended 31st March, 2021.

Bruce Ltd. is exploring the possibility of issuing preference shares to raise funds in the future. These preference shares would be redeemable at the option of the holder and would carry a fixed dividend payout of ₹ 12,000 per annum. However, Bruce Ltd. has decided to understand the accounting implications under IFRS before proceeding with the issuance.

Multiple Choice Questions:

- 3.1 Which one of the following is the appropriate classification for the annual payment of ₹ 12,000 on the proposed issuance of preference shares?
- (A) Dividend ₹ 12,000
 - (B) Interest Expense ₹ 12,000
 - (C) Dividend ₹ 3,000, Interest Expenses ₹ 9,000
 - (D) Dividend ₹ 9,000, Interest Expenses ₹ 3,000

- 3.2 *At the end of the 40-year period, Bruce Ltd. has a legally enforceable obligation to demolish the factory and restore the site to its original condition. Cost of demolition recognised as a provision would be:*
- (A) ₹ 4 crores
 - (B) ₹ 1.84 crores
 - (C) ₹ 18.4 lakhs
 - (D) ₹ 20 lakhs
- 3.3 *In respect of the loan given to Gulf Ltd., what is the income to be recognized by Bruce Ltd. in its standalone profit and loss account?*
- (A) ₹ 12,00,000 as interest income
 - (B) ₹ 12,00,000 as interest income and ₹ 4,00,000 as interest expense
 - (C) ₹ 7,00,000 as interest income and ₹ 1,00,000 as reimbursement of bank charges
 - (D) ₹ 11,00,000 as interest income and ₹ 3,00,000 as interest expense
- 3.4 *Calculate the closing balance of loan finance as at 31 March 2022 which Bruce Ltd. has raised from European investors.*
- (A) ₹ 848.30 crores
 - (B) ₹ 829.54 crores
 - (C) ₹ 833.00 crores
 - (D) ₹ 816.94 crores
- 3.5 *Calculate the exchange difference of loan finance from European investors to be recognized in profit or loss for the year ended 31st March, 2022.*
- (A) Gain- ₹ 31.36 crores
 - (B) Loss- ₹ 31.36 crores
 - (C) Loss- ₹ 44.70 crores
 - (D) Gain- ₹ 44.70 crores
- (5 x 2 Marks each = 10 Marks)**

Descriptive Questions

- 3.6 *Analyse the treatment of the Joint Arrangement with respect to the pipeline and calculate the borrowing cost, cost of asset, its depreciation and charge to the Statement of Profit or Loss of Bruce Limited and the other investor for the year ending 31st March, 2022.*

(4 Marks)

- 3.7 *Compute in the books of Bruce Ltd.:*
- (a) *the cost of factory*

- (b) depreciation on SLM basis thereon for the year ended 31st March, 2022
- (c) its carrying amount as at 31st March, 2022 **(6 Marks)**
- 3.8 Calculate the share based payment amounts to be included in the statement of financial position as at 31st March, 2022 and statement of profit & loss for the year then ended. **(5 Marks)**

Answer to Case Study 3

- 3.1 Option (b) : Interest expense ₹ 12,000
- 3.2 Option (c) : ₹ 18.4 lakhs
- 3.3 No Correct Option
- 3.4 Option (a) : ₹ 848.30 crores
- 3.5 Option (b) : Loss - ₹ 31.36 crores
- 3.6 Nature of joint arrangement

As provided in IFRS 11 'Joint Arrangements', this is a joint arrangement because two or more parties have joint control of the pipeline under a contractual arrangement.

The arrangement will be regarded as a joint operation because Bruce Ltd and the other investor have rights to the assets and obligations for the liabilities of this joint arrangement.

This means that Bruce Ltd and the other investor will each recognize 50% of the cost of constructing the asset in property, plant and equipment.

Calculation of borrowing cost

The borrowing cost incurred on constructing the pipeline should, under the principles of IAS 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 ₹ 10 lakhs (₹ 2 crores x 10% x 6/12).

Calculation of total cost of the asset

The total cost of the asset is ₹ 8.10 crores (₹ 8 crores + ₹ 10 lakhs).

₹ 4.05 crores will be included in the property, plant and equipment of Bruce Ltd. and the same amount in the property, plant and equipment of the other investor.

Calculation of depreciation charge

The depreciation charge for the year ended 31st March 2022 will therefore be ₹ 20.25 lakh (₹ 8.10 crores x 1/20 x 6/12).

₹ 10.125 lakhs will be charged in the Statement of profit or loss of Bruce Ltd. and the same amount will be charged in the Statement of profit or loss of the other investor.

Charge to Statement of Profit or Loss

The other costs relating to the arrangement in the current year totalling ₹ 18 lakhs (finance cost for the second half year of ₹ 10 lakhs plus maintenance costs of ₹ 8 lakhs) will be charged to the Statements of profit or loss of Bruce Ltd. and the other investor in equal proportions – ₹ 9 lakhs each.

3.7 Computation of the cost of the factory

Particulars	₹ in lakh
Purchase of land - both the purchase of land and the associated legal costs are direct costs of constructing the factory	200.00
Preparation and levelling - A direct cost of constructing the factory	6.00
Cost of materials - A direct cost of constructing the factory	121.60
Employment costs of construction workers - A direct cost of constructing the factory for a seven-month period	28.00
Direct overhead costs - A direct cost of constructing the factory for a seven-month period	14.00
Allocated overhead costs - Not a direct cost of construction	Nil
Income from use as a car park - Not essential to the construction so recognised directly in profit or loss	Nil
Finance costs - Capitalize the interest cost incurred in a seven-month period (purchase of land would not trigger off capitalization since land is not a qualifying asset. In fact, the construction started from 1 st May 2021) (W.N. 1)	10.65
Demolition cost recognised as a provision - Where an obligation must recognize as part of the initial cost	<u>18.40</u>
Total	<u>398.65</u>

Computation of accumulated depreciation

Particulars	₹ in lakh
Total depreciable amount (398.65 – 200 cost of land)	<u>198.65</u>
Note: All of the net finance cost of (10.65) has been allocated to the depreciable amount – as above	
Depreciation of roof : $198.65 \times 30\% \times 1/20 \times 4/12$	0.99325
Depreciation of remainder : $198.65 \times 70\% \times 1/40 \times 4/12$	<u>1.15879</u>
Total depreciation	<u>2.15204</u>

Computation of carrying amount of factory as at 31st March, 2022

Particulars	₹ in lakh
Cost of factory	398.65
Less: Depreciation	<u>(2.15204)</u>
Carrying amount of factory as at 31 st March, 2022	<u>396.49796</u>

Working Note 1:

Borrowing Cost	₹ in lakh
Loan amount	350
Interest for May to November (350 lakhs x 6% x 7/12)	12.25
Less: Income from Investment May to August (2 lakh x 4/5)	<u>(1.60)</u>
To be capitalised for 7 months from May to November	<u>10.65</u>

Note:

Alternatively, one may deduct full amount of interest income of investment from borrowing cost. The solution on that basis would be as follows:

Computation of the cost of the factory

Particulars	₹ in lakh
Purchase of land - both the purchase of land and the associated legal costs are direct costs of constructing the factory	200.00
Preparation and levelling - A direct cost of constructing the factory	6.00
Cost of materials - A direct cost of constructing the factory	121.60
Employment costs of construction workers - A direct cost of constructing the factory for a seven-month period	28.00
Direct overhead costs - A direct cost of constructing the factory for a seven-month period	14.00
Allocated overhead costs - Not a direct cost of construction	Nil
Income from use as a car park - Not essential to the construction so recognised directly in profit or loss	Nil
Finance costs - Capitalize the interest cost incurred in a seven-month period (purchase of land would not trigger off capitalization since land is not a qualifying asset. Infact, the construction started from 1 st May, 2021)	12.25

Investment income on temporary investment of the loan proceeds - Must offset against the amount capitalized	(2.00)
Demolition cost recognised as a provision - Where an obligation must recognize as part of the initial cost	<u>18.40</u>
Total	<u>398.25</u>

Computation of accumulated depreciation

Particulars	₹ in lakh
Total depreciable amount (398.25 – 200 cost of land)	<u>198.25</u>
Note: All of the net finance cost of (12.25 – 2.00) has been allocated to the depreciable amount – as above	
Depreciation of roof : $198.25 \times 30\% \times 1/20 \times 4/12$	0.9913
Depreciation of remainder : $198.25 \times 70\% \times 1/40 \times 4/12$	<u>1.1565</u>
Total depreciation	<u>2.1478</u>

Computation of carrying amount of factory as at 31st March, 2022

Particulars	₹ in lakh
Cost of factory	398.25
Less: Depreciation	<u>(2.1478)</u>
Carrying amount of factory as at 31st March, 2022	<u>396.1022</u>

- 3.8 In accordance with IFRS 2 'Share Based Payment', amount included in statement of financial position at 31st March 2022

Particulars	Amount
Number of executives - Expected to continue till 31 st March, 2022	190 Nos
Options vesting for each executive - Use expected number based on latest estimates as a non-market vesting condition	4,000
Impact of expected share price - This is a market-based vesting condition and is ignored for this purpose	None
Fair value of option - Use fair value on grant date as per IFRS 2	₹ 0.50
Proportion vesting - Two years through a three-year vesting period	2/3
Included in equity – (190 x 4,000 x ₹ 0.50 x 2/3)	₹ 2,53,333

Amount included in Statement of profit or loss and Other Comprehensive Income for the year ended 31st March 2022

Particulars	Amount (₹)
Cumulative amount recognised in equity at 31 st March 2022	2,53,333
Amount recognised in previous years – (200 x 3,000 x ₹ 0.50 x 1/3)	<u>(1,00,000)</u>
Included in current year's profit or loss	<u>1,53,333</u>

Case Study : 4

Wealth Ltd. is engaged in a number of businesses including automobiles, infrastructure and construction. The VP Finance has identified five segments (denoted as A to E below, for ease of reference).

Segments	Sales		Total Sales	Profit	Assets
	Exports	Domestic			
A	60,00,000		60,00,000	5,00,000	10,00,00,000
B	1,25,00,000	40,00,000	1,65,00,000	15,00,000	2,50,00,000
C	2,25,00,000		2,25,00,000	25,00,000	3,50,00,000
D	1,35,00,000	30,00,000	1,65,00,000	15,00,000	5,00,00,000
E	20,00,000	25,00,000	<u>45,00,000</u>	<u>10,00,000</u>	<u>7,50,00,000</u>
Total			<u>6,60,00,000</u>	<u>70,00,000</u>	<u>28,50,00,000</u>

Wealth Ltd. has an identifiable asset QR with a carrying amount of ₹20,00,000. Its recoverable amount is ₹13,00,000. The tax base of QR is ₹16,00,000 and the tax rate is 30%. Impairment losses are not tax deductible. Wealth Ltd. expects to continue to earn profits in future.

Wealth Ltd. acquired the trademark for a product from Czar Ltd. 10 years ago for ₹16,00,000. The trademark is expected to have an indefinite useful life. The carrying amount as on 1st April, 2021 is ₹16,00,000. Now due to competition, the sales of the product has declined by 25%. The management has made assessment and has ascertained that the trademark will continue to have indefinite useful life. However, the recoverable amount is ascertained to be ₹12,00,000.

Wealth Ltd. is proposing to acquire Health Ltd. which is currently following Indian GAAP (other than) the companies (Indian Accounting Standards) Rules 2015 Health Ltd. does not have taxable income as per the applicable tax laws, but pays 'Minimum Alternate Tax' (MAT) based on its books profits. The tax paid under MAT can be carried forward for the next 10 years and as per Health Ltd.'s projections submitted to its bankers, it is in a position to get credit for the

same by the end of eighth year. Health Ltd. is recognizing the MAT credit as a current asset under Indian GAAP. The amount of MAT credit as on 31st March, 2021 is ₹ 20,00,00,000 and as on 31 March, 2022 is ₹ 15,00,00,000. Management is looking for clarity on how these would be impacted upon conversion of Health Ltd.'s financial statements to IFRS once the acquisition goes through.

Wealth Ltd. has undertaken the following projects and follows percentage of completion method for its accounting purposes:

- Project 1-Contract value ₹ 1 crore and profit margin 20% on sales. At the end of the year 1, Wealth Ltd. has completed work and recognized revenue amounting to ₹ 50 lakhs while it has incurred a cost of ₹ 45 lakhs.
- Project 2 Contract value is ₹ 60 lakhs with a margin of 25% on sales. Wealth Ltd. has incurred expenditure of ₹ 4.5 lakhs which is yet to be certified by the client (as physical possession is not yet given). Management has also evaluated that the significant risks and rewards of the work done are yet to be transferred to the client.

Wealth Ltd. has entered into lease agreement with a lessor for a period of 5 years at the annual lease rental of ₹ 8 lakhs. There is an option at the end of the said period that lease can be owned by lessee. Other factors to be noted are discount rate of 8% per annum and interest rate of 10% per annum. At the end of the year 3, Wealth Ltd. exercised the option to purchase the land at value of ₹ 56 lakhs, whereas the market value on that date was ₹ 75 lakhs.

Wealth Ltd. has an immaterial subsidiary Mercury Ltd. The accountant of Mercury Ltd. has gathered the following data but needs assistance in preparing the statement of cash flows.

Particulars	2022	2021
	₹	₹
Cash	24,000	34,000
Accounts receivables	5,000	12,500
Prepaid insurance	15,000	17,000
Inventory	27,000	24,000
Fixed assets	3,16,000	2,70,000
Accumulated Depreciation	(45,000)	(30,000)
Total Assets	3,42,000	3,27,500
Accounts payable	15,000	14,000
Wages payable	7,000	9,000
Debentures	1,73,000	1,60,000
Equity shares	88,000	84,000

Retained earning	59,000	60,500
Total Liabilities and Equity	3,42,000	3,27,500
Sales	2,00,000	
COGS	(1,23,000)	
Other income	3,000	
Depreciation	(15,000)	
Insurance	(11,000)	
Auditors Expenses	(3,000)	
Wages	(50,000)	
Net Profit	1,000	

During 2022, Mercury Ltd. declared and paid dividends of ₹ 2,500 and paid cash of ₹ 46,000 to acquire new fixed assets. Accounts payable was used only for inventory and no debt was required during the year.

Multiple Choice Questions:

- 4.1 Based on the quantitative threshold, which of the above segments A to E would be considered as reportable segments?
- (A) Segment C
 (B) Segments C, D and B
 (C) Segments B, C, D and E
 (D) All are reportable segments
- 4.2 For the identifiable asset QR, what would be the closing balance of deferred tax asset/liability at the end of the period?
- (A) Deferred tax liability closing balance is ₹ 90,000
 (B) Deferred tax asset closing balance is ₹ 2,10,000
 (C) Deferred tax asset closing balance is ₹ 1,20,000
 (D) Deferred tax asset closing balance is ₹ 90,000
- 4.3 In respect of the trademark with indefinite life, Wealth Ltd. seeks your advice on the appropriate treatment from following:
- (A) Continue with the same carrying amount of ₹ 16,00,000
 (B) Adopt amortization policy for the amount of ₹ 12,00,000
 (C) Test the asset for impairment, as an external unfavorable event had occurred and reduce the carrying amount to ₹ 12,00,000

- (D) Test for impairment every year and accordingly, the carrying amount will be reduced to ₹ 12,00,000
- 4.4 In relation to Health Ltd., how will the MAT credit be recognised upon conversion to IFRS?
- (A) Current tax
 (B) Deferred Tax Asset (DTA)
 (C) Deferred Tax Liability (DTL)
 (D) Will not be recognised at all
- 4.5 In relation to Health Ltd., what will be the Deferred Tax Asset / Deferred Tax Liability (DTA/DTL) impact on account of MAT in the books of Wealth Ltd. for the year 2021-2022?
- (A) Increase in DTL by ₹ 5,00,000
 (B) Increase in DTA by ₹ 15,00,00,000
 (C) Increase in DTL by ₹ 15,00,00,000
 (D) Increase in DTA by ₹ 5,00,00,000 **(5 x 2 Marks each = 10 Marks)**

Descriptive Questions

- 4.6 Calculate the unbilled revenue/contract assets for the projects undertaken by Wealth Ltd. and determine the amount to be recognized in the financial statements. **(5 Marks)**
- 4.7 (i) Calculate the lease liability and right of use asset for the lease with the lessor. RoU is depreciated on SLM basis.
 (ii) Provide the amounts reflecting in the balance sheet, profit and loss and statement of cash flows at the end of year 1.
 (iii) What are the accounting entries if Wealth Ltd. decides to purchase the leased property at the end of year 3? **(6 Marks)**
- 4.8 Prepare the Statement of cash flows of Mercury Ltd. using the indirect method. **(4 Marks)**

Answer to Case Study 4

- 4.1 Option (D) : All are reportable segments
- 4.2 Option (D) : Deferred tax asset closing balance is ₹ 90,000
- 4.3 Option (D) – Test for impairment every year and accordingly, the carrying amount will be reduced to ₹ 12,00,000
- 4.4 Option (B) : Deferred Tax Asset (DTA)
- 4.5 No correct option

4.6 Computation of unbilled revenue/contract assets

		Project 1	Project 2
		₹	₹
Contract Value	A	1 crore	0.60 crore
Less: Profit margin on sales	B	0.20 crore	0.15 crore
Estimated cost	C	0.80 crore	0.45 crore
Cost incurred till date	D	0.45 crore	0.045 crore
Percentage of completion	E= [(D/C) x 100]	56.25%	10%
Revenue to be recognised	F= A x E	0.5625 crore	Nil
Less: Revenue recognised (billed)	G	0.50 crore	Nil
Unbilled revenue (to be recognised in the balance sheet) H=F - G		0.0625 crore	-
Contract asset (to be recognised in the balance sheet)		-	0.045 crore

Profit to be recognised in the books

	Project 1	Project 2
Revenue recognised (billed)	0.50 crore	Nil
Revenue for unbilled amount	<u>0.0625 crore</u>	<u>0.045 crore</u>
Total Revenue	0.5625 crore	0.045 crore
Less: Expenditure incurred till date	<u>(0.45 crore)</u>	<u>0.045 crore</u>
Profit / (Loss) for the year (to be recognised in the Statement of profit or loss)	<u>0.1125 crore</u>	<u>Nil</u>

With respect to Project 2, as per para 45 of IFRS 15, in some circumstances (for example, in the early stages of a contract), an entity may not be able to reasonably measure the outcome of a performance obligation, but the entity expects to recover the costs incurred in satisfying the performance obligation. In those circumstances, the entity shall recognise revenue only to the extent of the costs incurred until such time that it can reasonably measure the outcome of the performance obligation. Accordingly, ₹ 4.5 lakhs cost has also been recognised as revenue. However, since the work has yet not been certified, it will appear in the balance sheet as contract asset.

4.7 (i) Alternative 1

Assumptions used in the below given solution

- | | |
|----|--|
| 1. | Interest rate given in the question has been considered as the interest rate implicit in the lease. |
| 2. | At the beginning of the lease agreement, lessee is not reasonably certain to exercise the option. Hence, the exercise price has not been considered for determining the present value of the lease liability |

Calculation of ROU Asset and Lease Liability:

Year	Lease Payments/ Purchase Price	PVF @ 10%	PV of Lease payments
1	8,00,000	0.909	7,27,200
2	8,00,000	0.826	6,60,800
3	8,00,000	0.751	6,00,800
4	8,00,000	0.683	5,46,400
5	8,00,000	0.621	<u>4,96,800</u>
			<u>30,32,000</u>

Entity would amortise the right-of-use asset over the useful life of the underlying asset (5 years). Annual amortisation expense would be ₹ 6,06,400 (₹ 30,32,000 / 5 years). Accordingly, ROU Asset balance at the end of Year 1 is ₹ 24,25,600 (₹ 30,32,000-6,06,400).

(ii) Presentation at the end of Year 1:

In Balance Sheet	In Profit and Loss	In Statement of Cash Flows
ROU Asset: ₹ 24,25,600 (W.N.2)	Depreciation = ₹ 6,06,400 (W.N.2)	Cash flow from financing activities: Lease payment = ₹ 8,00,000
Lease Liability: ₹ 25,35,200 (W.N.1)	Interest expense (Finance cost) = ₹ 3,03,200 (W.N.1)	

- (iii) In the above part (i), it is assumed that lessee was not reasonably certain that he will exercise the option that's why the same has not been considered in determination of lease payment. Now, lessee is exercising the option at the end of 3rd year which implies that there is change in the assessment of an option to

purchase the underlying asset. Hence, paras 39 and 40(b) of IFRS 16 will come into the picture which are as follows (*only relevant part have been reproduced here*):

39 **After the commencement date**, a lessee shall apply paragraphs 40–43 to **remeasure the lease liability to reflect changes to the lease payments**. A lessee shall **recognise the amount of the remeasurement of the lease liability as an adjustment to the right-of-use asset**.

40 A lessee shall **remeasure the lease liability** by discounting the **revised lease payments** using a **revised discount rate**,

if either:

(a)

(b) **there is a change in the assessment of an option to purchase the underlying asset**, assessed considering the events and circumstances described in paragraphs 20–21 in the context of a purchase option. A lessee shall determine the revised lease payments to reflect the change in amounts payable under the purchase option.

In the question, in the absence of the information for revised discount rate, it is assumed that the interest rate implicit in the lease is same.

Therefore, the lease liability has to be remeasured on change in the assessment of exercising the option.

Original lease liability is ₹ 13,87,592 (Working Note 1). Since at the end of the 3rd year, the lease has been terminated due to exercise of option to purchase the asset, the revised lease liability is the amount paid on exercising the option i.e. ₹ 56,00,000. The difference of original lease liability and revised lease liability will increase the carrying amount of the right-of-use asset.

Accordingly, the adjustment to ROU Asset would be=₹ 56,00,000 - ₹ 13,87,592 = ₹ 42,12,408.

Journal Entry at the end of 3rd year

Particulars	Debit (₹)	Credit (₹)
ROU Asset	42,12,408	
To Lease liability		42,12,408
(Adjustment of difference in original lease liability and revised lease liability to ROU Asset)		

PPE	Dr.	54,25,608	
To ROU Asset (₹ 12,13,200 (Refer W.N.2) + ₹ 42,12,408)			54,25,608
(ROU Asset balance transferred to PPE on exercising of lease option)			
Lease Liability (₹ 42,12,408 + ₹ 13,87,592)	Dr.	56,00,000	
To Bank			56,00,000
(Purchase of land)			

Note: We have stopped till the entry to exercise the option to purchase the leased asset (as per the requirement of the question). Treatment for change in the value of PPE due to its fair value has not been considered here.

Working Note:

1. Calculation of outstanding Lease Liability at the end of 3rd year

Year	Opening balance (A)	Interest @ 10% (B)	Lease Payments (C)	Closing balance (A) + (B) - (C)
	₹	₹	₹	₹
1	30,32,000	3,03,200	8,00,000	25,35,200
2	25,35,200	2,53,520	8,00,000	19,88,720
3	19,88,720	1,98,872	8,00,000	13,87,592

2. Calculation of ROU Asset balance at the end of 3rd year

Year	Opening balance (A)	Depreciation (B)	Closing balance (A-B)
	₹	₹	₹
1	30,32,000	6,06,400	24,25,600
2	24,25,600	6,06,400	18,19,600
3	18,19,600	6,06,400	12,13,200

Alternative 2**Assumptions used in the below given solution**

1. Interest rate given in the question has been considered as the interest rate implicit in the lease.
2. Lessee is reasonably certain to exercise the option to purchase the leased asset at the end of lease term and ₹ 56,00,000 is the exercise price agreed in the lease term for purchasing of land at the end of the 5th year. Therefore, the same has been considered in computing the present value of the lease liability.

(i) Calculation of ROU Asset and Lease Liability:

Year	Lease Payments/ Purchase Price	PVF @ 10%	PV of Lease payments
1	8,00,000	0.909	7,27,200
2	8,00,000	0.826	6,60,800
3	8,00,000	0.751	6,00,800
4	8,00,000	0.683	5,46,400
5	64,00,000 (8,00,000 + 56,00,000)	0.621	<u>39,74,400</u>
			<u>65,09,600</u>

Entity would amortise the right-of-use asset over the useful life of the underlying asset (5 years). Annual amortisation expense would be ₹ 13,01,920 (₹ 65,09,600 / 5 years). Accordingly, ROU Asset balance at the end of Year 1 is ₹ 52,07,680 (₹ 65,09,600 - ₹ 13,01,920).

(ii) Presentation at the end of Year 1:

In Balance Sheet	In Profit and Loss	In Statement of Cash Flows
ROU Asset: ₹ 52,07,680 (W.N.2)	Depreciation = ₹ 13,01,920 (W.N.2)	Cash flow from financing activities: Lease payment = ₹ 8,00,000
Lease Liability: ₹ 63,60,560 (W.N.1)	Interest expense (Finance cost) = ₹ 6,50,960 (W.N.1)	

- (iii) In the above part (i), it is assumed that lessee was reasonably certain that he will exercise the option at the end of 5th year that's why the same has been considered in determination of lease payment. Now, lessee is exercising the option at the end

of 3rd year which implies that there is **change in the assessment of an option** to purchase the underlying asset. Hence, paras 39 and 40(b) of IFRS 16 will come into the picture which are as follows (*only relevant part have been reproduced here*):

39 **After the commencement date**, a lessee shall apply paragraphs 40–43 to **remeasure the lease liability to reflect changes to the lease payments**. A lessee shall **recognise the amount of the remeasurement of the lease liability as an adjustment to the right-of-use asset**.

40 A lessee shall **remeasure the lease liability** by discounting the **revised lease payments** using a **revised discount rate**,

if either:

(a)

(b) **there is a change in the assessment of an option to purchase the underlying asset**, assessed considering the events and circumstances described in paragraphs 20–21 in the context of a purchase option. A lessee shall determine the revised lease payments to reflect the change in amounts payable under the purchase option.

In the question, in the absence of the information for revised discount rate, it is assumed that the interest rate implicit in the lease is same.

Therefore, the lease liability has to be remeasured on change in the assessment of exercising the option.

Original lease liability is ₹ 60,16,278 (Working Note 1). Since at the end of the 3rd year, the lease has been terminated due to exercise of option to purchase the asset, the revised lease liability is the amount paid on exercising the option i.e. ₹ 56,00,000. The difference of original lease liability and revised lease liability will decrease the carrying amount of the right-of-use asset.

Accordingly, the adjustment to ROU Asset would be = ₹ 60,16,278 – ₹ 56,00,000
= ₹ 4,16,278.

Journal Entry

Particulars	Debit (₹)	Credit (₹)
Lease liability Dr.	4,16,278	
To ROU Asset		4,16,278
(Adjustment of difference in original lease liability and revised lease liability to ROU Asset)		

PPE	Dr.	21,87,562	
To ROU Asset (₹ 26,03,840 (Refer W.N.2) - ₹ 4,16,278)			21,87,562
(ROU Asset balance transferred to PPE on exercising of lease option)			
Lease Liability	Dr.	56,00,000	
To Bank/Lease payable			56,00,000
(Extinguishment of lease liability)			

Note: We have stopped till the entry to exercise the option to purchase the leased asset (as per the requirement of the question). Treatment for change in the value of PPE due to its fair value has not been considered here.

Working Note

1. Calculation of outstanding Lease Liability at the end of 3rd year

Year	Opening balance (A)	Interest @ 10% (B)	Lease Payments (C)	Closing balance (A) + (B) - (C)
	₹	₹	₹	₹
1	65,09,600	6,50,960	8,00,000	63,60,560
2	63,60,560	6,36,056	8,00,000	61,96,616
3	61,96,616	6,19,662	8,00,000	60,16,278

2. Calculation of ROU Asset balance at the end of 3rd year

Year	Opening balance (A)	Depreciation (B)	Closing balance (A-B)
	₹	₹	₹
1	65,09,600	13,01,920	52,07,680
2	63,60,560	13,01,920	39,05,760
3	61,96,616	13,01,920	26,03,840

4.8

Statement of Cash Flows for the year ended 31st March 2022

(Indirect method)

Particulars	₹	₹
Cash flow from operating activities:		
Net Profit	1,000	

Add: Depreciation	<u>15,000</u>	
Operating profit before working capital changes	16,000	
Decrease in trade receivables	7,500	
Prepaid Insurance	2,000	
Increase in inventories	(3,000)	
Increase in Accounts payable	1,000	
Decrease in wages payables	<u>(2,000)</u>	
<i>Net cash from operations</i>		21,500
Cash from investing activities:		
Purchase of fixed assets	<u>(46,000)</u>	
<i>Net cash used for investment activities</i>		(46,000)
Cash flows from financing activities:		
Issue of Debentures	13,000	
Issue of share capital	4,000	
Dividends paid	<u>(2,500)</u>	
<i>Net cash from financing activities</i>		<u>14,500</u>
Net decrease in cash and cash equivalents		(10,000)
Cash and cash equivalents as on 31 st March, 2021		<u>34,000</u>
Cash and cash equivalents as on 31 st March, 2022		<u>24,000</u>

Case Study : 5

Star Ltd. is engaged in the business of providing solar and alternative energy. On 1st April, 2021, Star Ltd. received a loan for ₹ 25,00,000 from the government @10% per annum payable after 5 years in a bulleted payment. The prevailing market rate of interest is 20% per annum. Interest is payable regularly at the end of each year.

Star Ltd. is in the process of amalgamation with Venus Ltd. The Company determines the valuation on the measurement date (31st March, 2022) as per Market Approach and Income Approach and assign equal weight to both the approaches The valuation and other details of Star Ltd. are as follows:

Particulars	₹ in crore
Valuation as per Market Approach	5,000

Valuation as per Income Approach	3,000
Debt obligation as on measurement date	1,200
Surplus cash and cash equivalents	120
Fair value of surplus assets and liabilities	300
Number of shares of Star Ltd.	7,50,00,000 shares

Star Ltd. is commencing a new construction project, which is to be financed by borrowings. The key dates are as follows:

- 16 June 2021: Loan interest relating to the project starts to be incurred
- 3 July 2021: Technical site planning commences
- 20 July 2021: Expenditure on the projects started to be incurred
- 19 August 2021: Construction work commences

Star Ltd. purchased a deluxe property, depreciated on SLM basis, for ₹ 12,00,000 on 1st April, 2019. The useful life of this property is 15 years. On 30th March, 2021, Star Ltd. classified the property as held for sale. The impairment testing provides the estimated recoverable amount of ₹ 9,40,000. The fair value less cost to sell on 31st March, 2021 was ₹ 9,20,000. On 31st March, 2022, management changes the plan, as this property no longer met the criteria of held for sale. The recoverable amount as at 31st March, 2022 is estimated to be ₹ 10,00,000.

As on 1st April, 2021, the Company's fair value of plan assets was ₹ 20,000 lakhs. Contribution to the plan assets done 31st March, 2022 was ₹ 6,000 lakhs. Amount paid out on 31st March, 2022 was ₹ 600 lakhs. As on 31st March, 2020, the fair value of plan assets was ₹ 29,400 lakhs and actual return on the plan assets was ₹ 4,000 lakhs.

As on 1st April, 2021, present value of the defined benefit obligation was ₹ 24,000 lakhs. At 31st March, 2022, present value of the defined benefit obligation was ₹ 31,000 lakhs. Actuarial losses on the obligation for the year ended 31st March, 2022 were ₹ 200 lakhs. Current service cost was ₹ 5,000 lakhs. Benefit paid was ₹ 600 lakhs. Discount rate used to calculate defined benefit liability is 10% per annum.

Star Ltd. has three cash generating units P, Q and R, the carrying amounts of which are as follows as on 31st March 2022:

Cash generating units	Carrying amount (₹ in Crore)	Remaining useful life (years)
P	1,000	10
Q	1,500	20
R	2,200	20

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

₹ in Crore		
Corporate Assets	Carrying Amount	Remarks
A	1200	The carrying amount of A can be allocated on a reasonable basis (i.e pro-rata basis) to the individual cash generating units
B	400	The carrying amount of B cannot be allocated on a reasonable basis to the individual cash generating units.

Recoverable amount as on 31st March, 2022 is as follows:

Cash Generating Units	Recoverable amount (₹ in Crore)
P	1,200
Q	1,800
R	2,800
Star Ltd.	6,400

The Board of Directors of Star Ltd. authorized the financial statements for the reporting period 2021-2022 for issue on 16th July, 2022. The management of Star Ltd. discovered a major fraud and decided to reopen the books of account. The financial statements were subsequently authorized by the Board of Directors on 31st July, 2022. Its annual general meeting for the reporting period was held on 13th August, 2022.

Multiple Choice Questions:

- 5.1 Calculate the amount of government grant and fair valuation of loan received from the government.
- (A) Government Grant - ₹ 25,00,000 and Fair Valuation of loan - ₹ NIL
 (B) Government Grant - ₹ 7,47,600 and Fair Valuation - ₹ 17,52,400
 (C) Government Grant - ₹ 6,25,893 and Fair Valuation - ₹ 18,74,107
 (D) Government Grant - Nil and Fair Valuation - ₹ 25,00,000
- 5.2 Determine the equity value of one share of Star Ltd. as on the measurement date using the valuation and other details of Star Ltd.
- (A) ₹ 666.67
 (B) ₹ 533.33
 (C) ₹ 429.33
 (D) ₹ 439.33

- 5.3 Identify the commencement date of new construction project
- (A) 16th June, 2021
 - (B) 3rd July, 2021
 - (C) 20th July, 2021
 - (D) 19th August, 2021
- 5.4 Amongst the following, which one is not a fair valuation approach under IFRS?
- (A) Margin Approach
 - (B) Cost Approach
 - (C) Income Approach
 - (D) Market Approach
- 5.5 What is the date of authorization to be considered for the issue of financial statements by the Board of Directors?
- (A) 31st March, 2022
 - (B) 16th July, 2022
 - (C) 31st July, 2022
 - (D) 13th August, 2022
- (5 x 2 Marks each = 10 Marks)**

Descriptive Questions

- 5.6 Based on Star Ltd.'s employee benefit obligations described above, calculate the amount to be taken to other comprehensive income for re-measurement, with detailed workings. Also compute the net interest on not defined benefit liability/asset. **(3 Marks)**
- 5.7 What is the value of the deluxe property as at end of 31st March, 2021 and 31st March, 2022? Discuss the accounting treatment and amount of impairment loss in the Statement of Profit or Loss for the year ended 31st March, 2021 and 31st March, 2022. **(4 Marks)**
- 5.8 Calculate the impairment loss of all cash generating units (P, Q and R) and Star Ltd. as a whole, if any. **(8 Marks)**

Answer to Case Study 5

- 5.1 Option (B) : Government Grant - ₹ 7,47,600 and Fair valuation ₹ 17,52,400
- 5.2 Option (C) : ₹ 429.33
- 5.3 Alternative 1 Option (C) : 20th July 2021 (Commencement date for capitalisation of borrowing cost of new construction project)

Alternative 2 Option (B) : 3 July 2021 (Commencement date of new construction project)

5.4 Option (A) : Margin approach

5.5 Option (C) : 31st July, 2022

5.6 (i) Computation of amount of remeasurement

Particulars	₹
Actual return on plan asset for the year ended 31 st March 2022 (C)	4,000
Less: Interest income on ₹ 20,000 held for 12 months at 10% (D)	<u>(2,000)</u>
Remeasurement (E = C - D)	<u>2,000</u>

Computation of net remeasurement = Remeasurement – Actuarial loss
 = ₹ 2,000 – ₹ 200 = ₹ 1,800.

As per IAS 19, net remeasurement of ₹ 1,800 would be recognized in Other Comprehensive Income.

(ii) Computation of net interest expense

Particulars	₹
Defined benefit liability as at 1 st April 2021 (A)	24,000
Fair value of plan asset as at 1 st April 2021 (B)	<u>(20,000)</u>
Net defined benefit liability (A - B)	<u>4,000</u>
Net interest expense (as it is net liability) (Refer note given below)	<u>400</u>

Working Note:

Net interest expense would be computed on net defined benefit liability using discount rate of 10% = Net defined benefit liability x Discount rate

$$= ₹ 4,000 \times 10\%$$

$$= ₹ 400.$$

5.7 (a) Value of property immediately before the classification as held for sale as per IAS 16 as on 31st March, 2021 ₹

Purchase Price	12,00,000
Less: Accumulated Depreciation (for two years)	<u>1,60,000</u>
Carrying value as on 31 st March 2021 before impairment	10,40,000
Less: Impairment loss (10,40,000-9,40,000)	<u>1,00,000</u>

Carrying Amount after impairment loss before classification as held for sale	<u>9,40,000</u>
--	-----------------

On initial classification as held for sale on 31st March, 2021, the value of property will be lower of:

Carrying amount after impairment	₹ 9,40,000
Fair Value less cost to sell	₹ 9,20,000

On 31st March 2021, Non-current asset classified as held for sale will be recorded at ₹ 9,20,000.

Depreciation of ₹ 80,000 and Impairment Loss of ₹ 1,20,000 (1,00,000 +20,000) is charged to profit or loss for the year ended 31st March 2021.

- (b) On 31st March 2022, held for sale property is reclassified as PPE since criteria for classification as held for sale does not meet. The value will be lower of:

Carrying amount immediately before classification on 31 st March 2021	₹ 9,40,000
Less: Depreciation based on 13 years balance life	<u>(₹ 72,308)</u>
Carrying amount had the asset is not classified as held for sale	₹ 8,67,692
Recoverable Amount	₹ 10,00,000

Property will be valued at ₹ 8,67,692 on 31st March 2022

Adjustment to the carrying amount of ₹ 52,308 (₹ 9,20,000 – ₹ 8,67,692) is charged to the profit or loss since this reversal is less than total impairment loss of ₹ 1,20,000.

5.8 Allocation of corporate assets

The carrying amount of Corporate Asset 'A' 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 P's cash-generating unit is 10 years, whereas the estimated remaining useful lives of Q and R's cash-generating units are 20 years.

(₹ in crore)				
Particulars	P	Q	R	Total
Carrying amount (i)	1,000	1,500	2,200	4,700
Useful life	10 years	20 years	20 years	—
Weight based on useful life	1	2	2	—
Carrying amount (after assigning weight)	1,000	3,000	4,400	8,400

Pro-rata allocation of Corporate Asset 'A'	12% (1,000/8,400)	36% (3,000/8,400)	52% (4,400/8,400)	100%
Allocation of carrying amount of Corporate Asset 'A' (ii)	<u>144</u>	<u>432</u>	<u>624</u>	<u>1,200</u>
Carrying amount (after allocation of A)	<u>1,144</u>	<u>1,932</u>	<u>2,824</u>	<u>5,900</u>

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	P	Q	R
Carrying amount (after allocation of Corporate Asset 'A')	1,144	1,932	2,824
Recoverable amount	<u>1,200</u>	<u>1,800</u>	<u>2,800</u>
Impairment loss	<u>-</u>	<u>132</u>	<u>24</u>

(b) Allocation of the impairment loss

(₹ in crore)				
Allocation to	Q		R	
Corporate Asset 'A'	30	(132 x 432/1932)	5	(24 x 624/2,824)
Other assets in cash-generating units	<u>102</u>	(132 x 1500/ 1932)	<u>19</u>	(24 x 2,200/ 2,824)
Impairment loss	<u>132</u>		<u>24</u>	

Step II: Impairment losses for the larger cash-generating unit, i.e., Star Ltd. as a whole

(₹ in crore)						
Particulars	P	Q	R	A	B	Star Ltd.
Carrying amount	1,000	1,500	2,200	1,200	400	6,300
Impairment loss (Step I)	—	(102)	(19)	(35)	—	(156)
Carrying amount (after Step I)	1,000	1,398	2,181	1,165	400	6,144
Recoverable amount						6,400
Impairment loss for the 'larger' cash-generating unit						Nil