J.K. SHAH TEST SERIES
Evaluate Learn Succeed

CA FINAL – Nov'19

SUBJECT- FR

Test Code – FNJ 7166

(Date :)

(Marks - 100)

Question 1 is compulsory and attempt any four out of remaining five questions

Question 1:

(A)

How contingent consideration payable in relation to a **business combination** should be accounted for on initial recognition and at the subsequent measurement **as per Ind AS** in the following cases:

i) On 1 April 2016, A Ltd. acquires 100% interest in B Ltd. As per the terms of agreement the purchase consideration is payable in the following 2 tranches:

- an immediate issuance of 10 lakhs shares of A Ltd. having face value of INR 10 per share;
- a further issuance of 2 lakhs shares after one year if the profit before interest and tax of B Ltd. for the first year following acquisition exceeds INR 1 crore.

The fair value of the shares of A Ltd. on the date of acquisition is INR 20 per share. Further, the management has estimated that on the date of acquisition, the fair value of contingent consideration is Rs. 25 lakhs.

During the year ended 31 March 2017, the profit before interest and tax of B Ltd. exceeded Rs. 1 crore. As on 31 March 2017, the fair value of shares of A Ltd. is Rs. 25 per share.

ii) Continuing with the fact pattern in (a) above except for:

- The number of shares to be issued after one year is not fixed.
- Rather, A Ltd. agreed to issue variable number of shares having a fair value equal to Rs. 40 lakhs after one year, if the profit before interest and tax for the first year following acquisition exceeds Rs. 1 crore. A Ltd. issued shares with Rs. 40 lakhs after an year. **(12 marks)**

(B)

The following balances and information are extracted from Induga Ltd. as at 31st December 2017

	Current Value (Amt. in Rs.)	Tax Base (Amt. in Rs.)
Non-current assets		
Assets subject to investment relief	63,000	
Land	2,00,000	
Plant and Equipment	1,00,000	90,000

Receivable	
Trade receivables	73,000
Interest receivable	1,000
Payables	
Fine	10,000
Interest Payable	3,300

Additional information:

1. The asset having carrying value of Rs. 63,000 cost to company RS. 70,000 at the start of the year. It is being depreciated on a 10% straight line basis for accounting purposes. Company's tax advisers have said that the company can claim Rs. 42,000 as a taxable expense in this year's tax computation.
2. The land has been revalued during the year in accordance with Ind AS-16, Property, Plant and Equipment. It originally cost Rs. 1,50,000. Land is not subject to depreciation under Ind AS.
3. The balances in respect of plant and equipment are after allowing for accounting depreciation of Rs. 12,000 and tax allowable deprecation of Rs. 10,000 respectively.
4. The trade receivables balance in the accounts is made up of the following:

Balances	Rs. 80,000
Allowances	Rs. (7,000)
	Rs. 73,000

5. The balance on the deferred taxation account (liability) on 1st January 2017 was Rs. 3,600.
6. The applicable tax rate is 30%
7. Interest is allowable / taxable on cash basis.

Required:

(a) **Identify the tax base item** listed and then identify the temporary difference.

(b) **Calculate the deferred tax provision** required at 31st December 2017 and the charge to profit or loss in respect of deferred taxation for the year. **(8 marks)**

Question 2:

(A)

On 1st April 2015 MK Ltd **granted share options** to 20 senior executives. The options are due to vest on 31st March 2018 provided the senior executives remain with the company for that period. The number of options vesting to each director depends on the cumulative profits over the 3-year period from 1st April 2015 to 31st March 2018:

- 10,000 options per director if the cumulative profits are between Rs. 50 lakhs and rupees one crore.
- 15,000 options per director if the cumulative profits are more than rupees one crore

On 1st April 2015 and 31st March 2016 the best estimate of the cumulative profits for the 3-year period ending on 31st March 2018 was Rs. 80 lakhs. However, the following very successful result in the year ended 31st March 2017; the latest estimate of the cumulative profits in the relevant 3-year period is Rs. 1,40,00,000.

On 1st April 2015 it was estimated that all 20 senior executives would remain with MK Ltd for the 3-year period, but on 31st December 2015 one senior executive left unexpectedly. None of the other executives have since left and none are expected to leave before 31st March 2018.
A further condition for vesting of the options is that the share price of MK Ltd should be at least Rs. 12 on 31st March 2018. The share price of MK Ltd over the last 2-years has changed follows:

- Rs. 10 on 1st April 2015;
- Rs. 11.75 on 31st March 2016;
- Rs. 11 .25 on 31st March 2017

On 1st April 2015 the fair value of the share options granted by MK Ltd was Rs. 4.80 per option. This had increased to Rs. 5.50 by 31st March 2016 and Rs. 6.50 by 31st March 2017.

Required:

Produce **extracts**, with supporting explanations, from Balance Sheet at 31st March 2016 and 2017 and from the statement of profit and loss for the years ended 31st March 2016 and 2017 that show how this transaction will be reflected in the financial statements of MK Ltd.

Your calculation should be as per relevant Ind AS. **(6 marks)**

(B)

A Limited received from the **government a loan** of Rs.1,00,00,000 @ 5% payable after 5 years in a bulleted payment. The prevailing market rate of interest is 12%. Interest is payable regularly at the end of each year. Calculate the amount of **government grant** and Pass necessary **journal entry**. Also examine how the Government grant be realized. Also state how the grant will be recognized in the statement of profit or loss assuming that the loan is to finance a depreciable asset. **(5 marks)**

(C)

A Ltd. prepares its financial statements to 31st March each year. It operates a **defined benefit retirement benefits plan** on behalf of current and former employees. A Ltd. receives advice from actuaries regarding contribution levels and overall liabilities of the plan to pay benefits. On 1st April, 2017, the actuaries advised that the present value of the defined benefit obligation was Rs.6,00,00,000. On the same date, the fair value of the assets of the defined benefit plan was Rs. 5,20,00,000. On 1st April, 2017, the annual market yield on government bonds was 5%. During the year ended 31st March, 2018, A Ltd. made contributions of Rs. 70,00,000 into the plan and the plan paid out benefits of Rs. 42,00,000 to retired members. Both these payments were made on 31st March, 2018.

The actuaries advised that the current service cost for the year ended 31st March, 2018 was Rs. 62,00,000. On 28th February, 2018, the rules of the plan were amended with retrospective effect. These amendments meant that the present value of the defined benefit obligation was increased by Rs. 15,00,000 from that date.

During the year ended 31st March, 2018, A Ltd. was in negotiation with employee representatives regarding planned redundancies. The negotiations were completed shortly before the year end and redundancy packages were agreed. The impact of these redundancies was to reduce the present value of the defined benefit obligation byRs. 80,00,000. Before 31st March, 2018, A Ltd. made payments of Rs. 75,00,000 to the employees affected by the redundancies in compensation for the curtailment of their benefits. These payments were made out of the assets of the retirement benefits plan.

On 31st March, 2018, the actuaries advised that the present value of the defined benefit obligation was Rs. 6,80,00,000. On the same date, the fair value of the assets of the defined benefit plan were Rs. 5,60,00,000.

Examine and present **how the above event would be reported** in the financial statements of A Ltd. for the year ended 31st March, 2018 as per Ind AS. **(6 marks)**

(D)

Differentiate between **Financial capital maintenance and Physical capital maintenance** as per the Framework. **(3 marks)**

Question 3(A):

Angel Ltd. has adopted Ind AS with a transition date of 1st April, 2017. Prior to Ind AS adoption, it followed Accounting Standards notified under Companies (Accounting Standards) Rules, 2006 (hereinafter referred to as "IGAAP").

It has made investments in equity shares of Pharma Ltd., a listed company engaged in the business of pharmaceuticals. The shareholding pattern of Pharma Ltd. is given below:

Shareholders (refer Note 1)	Percentage shareholding as on 1st April, 2017
Angel Ltd.	21%
Little Angel Ltd. (refer Note 2)	24%
Wealth Master Mutual Fund (refer Note 3)	3%
Individual public shareholders (refer Note 4)	52%

Notes:

(1) None of the shareholders have entered into any shareholders' agreement.

(2) Little Angel Ltd. is a subsidiary of Angel Ltd. (under Ind AS) in which Angel Ltd. holds 51% voting power.

(3) Wealth Master Mutual Fund is not related party of either Little Angel Ltd. or Pharma Ltd.

(4) Individual public shareholders represent 17,455 individuals. None of the individual shareholders hold more than 1% of voting power in Pharma Ltd.

All commercial decisions of Pharma Ltd. are taken by its directors who are appointed by a simple majority vote of the shareholders in the annual general meetings ("AGM ”). The following table shows the voting pattern of past AGMs of Pharma Ltd.:

Shareholders	AGM for the financial year: 2013-14	2014-15	2015-16
Angel Ltd.	Attended and voted in favour of all the resolutions	Attended and voted in favour of all the resolutions	Attended and voted in favour of all the resolutions
Little Angel Ltd.	Attended and voted as per directions of Angel Ltd.	Attended and voted as per directions of Angel Ltd	Attended and voted as per directions of Angel Ltd

Wealth Master Mutual Fund	Attended and voted in favour of all the resolutions except for the reappointment of the retiring directors	Attended and voted in favour of all the resolutions except for the reappointment of the retiring directors	Attended and voted in favour of all the resolutions except for the reappointment of the retiring directors
Individuals	7% of the individual shareholders attended the AGM. All the individual shareholders voted in favour of all the resolutions, except that 50% of the individual Shareholders voted against the resolution to appoint the retiring directors.	8% of the individual shareholders attended the AGM. All the individual shareholders voted in favour of all the resolutions, except that 50% of the individual Shareholders voted against the Resolution to appoint the retiring directors.	6% of the individual shareholders attended the AGM. All the individual shareholders voted in favour of all the resolutions, except that 50% of the individual Shareholders voted against the resolution to appoint the retiring directors.

Pharma Ltd. has obtained substantial long term borrowings from a bank. The loan is payable in 20 years from 1st April, 2017. As per the terms of the borrowing, following actions by Pharma Ltd. will require prior approval of the bank:

- Payment of dividends to the shareholders in cash or kind;
- Buyback of its own equity shares;
- Issue of bonus equity shares;
- Amalgamation of Pharma Ltd. with any other entity; and
- Obtaining additional loans from any entity.

Recently, the Board of Directors of Pharma Ltd. proposed a dividend of *Rs.* 5 per share. However, when the CFO of Pharma Ltd. approached the bank for obtaining their approval, the bank rejected the proposal citing concerns over the short-term cash liquidity of Pharma Ltd. Having learned about the developments, the Directors of Angel Ltd. along with the Directors of Little Angel Ltd. approached the bank with a request to re-consider its decision. The Directors of Angel Ltd. and Little Angel Ltd. urged the bank to approve a reduced dividend of at least *Rs.* 2 per share. However, the bank categorically refused to approve any payout of dividend.

Under IGAAP, Angel Ltd. has classified Pharma Ltd. as its associate. As the CFO of Angel Ltd., **you are required to comment on the correct classification of Pharma Ltd. on transition to Ind AS.**

(15 marks)

(B) A building is used for CSR activities of the company. The same is capitalised as 'an asset' in the books and depreciation is charged on the same as per the Companies Act, 2013.

The Company claims the cost of the building as '**CSR expenditure**' and also the depreciation thereon.

Required:

Is this the **correct treatment** as per the Act? **(5 marks)**

Question 4:

(A)

Asset A is a contractual right to receive Rs. 1000 after one year. Asset B is a contractual right to receive Rs. 1250 in two years and has a market price of Rs. 1080. **How the discount rate adjustment technique should be applied to Asset A**. There is no comparable asset which matures in one year. The zero coupon yield curve on government securities two years rate is 40bp higher than one year rate. **(4 marks)**

(B)

The building, if purchased outright, would have a useful economic life of 50 years. The lease term, which would commence on 1 January 2019, is for 30 years. D Ltd would pay 40% of the asset's value upfront. At the end of each of the 30 years, there is also an annual rental payment due. This is equivalent to 6% of the asset's value as at 1 January 2019 or a contingent rent, if higher, at the year end. Legal title at the end of the lease remains with the lessor, but D Ltd can continue to lease the asset indefinitely at a rental that is substantially below its market value. If D Ltd cancels the lease, it must make a payment to the lessor to recover their remaining investment.

As per **Ind AS 17 Leases**, should the **lease be classified as an operating lease or a finance lease**? **(6 marks)**

(C) On 1^{st} April, 2014, S Ltd. issued 5,000, 8% convertible debentures with a face value of Rs. 100 each maturing on 31^{st} March, 2019. The debentures are convertible into equity shares of S Ltd. at a conversion price of Rs. 105 per share. Interest is payable annually in cash. At the date of issue, S Ltd. could have issued non-convertible debentures with a 5 year term bearing a coupon interest rate of 12%. On 1^{st} April, 2017, the convertible debentures have a fair value of Rs. 5,25,000. S Ltd. makes a tender offer to debenture holders to repurchase the debentures for Rs. 5,25,000, which the holders accepted. At the date of repurchase, S Ltd. could have issued non-convertible debt with a 2 year term bearing a coupon interest rate of 9%.

Examine the accounting treatment in the books of S Ltd., by passing appropriate journal entries, for recording of equity and liability component:

(1) At the time of initial recognition and

(2) At the time of repurchase of the convertible debentures.

The following present values of Re. 1 at 8%, 9% & 12% are supplied to you:

Interest Rate	Year 1	Year 2	Year 3	Year 4	Year 5
8%	0.926	0.857	0.794	0.735	0.681
9%	0.917	0.842	0.772	0.708	0.650
12%	0.893	0.797	0.712	0.636	0.567

(10 marks)

Question 5:

(A)

ABC changed its accounting policy for inventory in 2016-2017. Prior to the change, inventory had been valued using the first in first out method (FIFO). However, it was felt that in order to match current practice and to make the financial statements more relevant and reliable a weighted average valuation model should be used.

The effect of the change on the valuation of inventory was as follows:

- 31st March, 2015 - Increase of Rs. 10 million
- 31st March, 2016 - Increase of Rs. 15 million
- 31st March, 2017- Increase of Rs. 20 million

Profit or loss under the FIFO valuation model are as follows: Rs. in million

	2016-2017	**2015-2016**
Revenue	324	296
Cost of sales	(173)	(164)
Gross profit	**151**	**132**
Expenses	(83)	(74)
Profit	**68**	**58**

Retained earnings at 31st March, 2015 were Rs. 423 million.

Present the change in accounting policy in the profit or loss and produce an extract of the statement of changes in equity in accordance with Ind AS 8. **(5 marks)**

(B)

Seeds Ltd. is operating in oil industry. Its business segments comprise crushing and refining. Certain information for financial year 2017-18 is given below:

(Rs. in lakh)

Segments	***External Sale***	***Tax***	***Other Operating Income***	***Result***	***Assets***	***Liabilities***
Crushing	*1,00,000*	*2,500*	*20,000*	*5,000*	*25,000*	*15,000*
Refining	*35,000*	*1,500*	*7,500*	*2,000*	*15,000*	*5,000*

Additional Information: (Rs. in lakh)

- Unallocated revenue net of expenses is Rs. 1,500.
- Interest and bank charges is Rs. 1,000
- Income-tax expense is Rs. 1,000 (current tax Rs. 975 and deferred tax Rs. 25)
- Investments Rs. 5,000 and unallocated assets Rs. 5,000
- Unallocated liabilities, Reserves & Surplus and Share capital are Rs. 10,000; Rs. 15,000 and Rs. 5,000 respectively.
- Depreciation amounts for crushing and refining are Rs. 500 and Rs. 150 respectively.

– Capital expenditure for crushing and refining are Rs. 2,500 and Rs. 1,000 respectively.

- Revenue from outside India is Rs. 15,000 and segment assets outside India Rs. 5,000.

Based on the above information, how Seeds Ltd. would disclose information about reportable segment revenue, profit or loss, assets and liabilities for financial year 2017-18?

(10 marks)

(C)

Deluxe bike manufactured by Zed Limited is sold with an extended warranty of 2 years for Rs. 87,300 while an identical Deluxe bike without the extended warranty is sold in the market for Rs. 80,000 and equivalent warranty is given in the market for Rs. 10,000. How should Zed Limited recognize and measure revenue in the books on the sale of the bikes and warranty?

(5 marks)

Question 6:

(A)

A Ltd. intends to open a new retail store in a new location in the next few weeks. It has spent a substantial sum on a series of television advertisements to promote this new store. It has paid for advertisements costing Rs. 8,00,000 before 31st March, 2018. Rs. 7,00,000 of this sum relates to advertisements shown before 31st March, 2018 and Rs. 1,00,000 to advertisements shown in April, 2018. Since 31st March, 2018, A Ltd. has paid for further advertisements costing Rs. 4,00,000. The accountant charged all these costs as expenses in the year to 31 March 2018. However, CFO of A Ltd. does not want to charge Rs.12,00,000 against 2017-2018 profits. He believes that these costs can be carried forward as intangible assets because the company's market research indicates that this new store is likely to be highly successful.

Examine and justify the treatment of these costs of Rs. 12,00,000 in the financial statements for the year ended 31st March, 2018 as per Ind AS. **(4 marks)**

(B)

U Ltd. is a large conglomerate with a number of subsidiaries. It is preparing consolidated financial statements as on 31st March 2018 as per the notified Ind AS. The financial statements are due to be authorised for issue on 15th May 2018. It is seeking your assistance for some transactions that have taken place in some of its subsidiaries during the year.

G Ltd. is a wholly owned subsidiary of U Ltd. engaged in management consultancy services. On 31st January 2018, the board of directors of U Ltd. decided to discontinue the business of G Ltd. from 30th April 2018. They made a public announcement of their decision on 15th February 2018.

G Ltd. does not have many assets or liabilities and it is estimated that the outstanding trade receivables and payables would be settled by 31st May 2018. U Ltd. would collect any amounts still owed by G Ltd's customers after 31st May 2018. They have offered the employees of G Ltd. termination payments or alternative employment opportunities.

Following are some of the details relating to G Ltd.:

On the date of public announcement, it is estimated by G Ltd. that it would have to pay 540 lakhs as termination payments to employees and the costs for relocation of employees who would remain with the Group would be Rs. 60 lakhs. The actual termination payments totalling to Rs. 520 lakhs were made in full on 15th May 2018. As per latest estimates made on 15th May 2018, the total relocation cost is Rs. 63 lakhs.

G Ltd. had taken a property on operating lease, which was expiring on 31st March 2022. The present value of the future lease rentals (using an appropriate discount rate) is Rs. 430 lakhs. On 15th May 2018, G Ltd. made a payment to the lessor of Rs. 410 lakhs in return for early termination of the lease.

The loss after tax of G Ltd. for the year ended 31st March 2018 was Rs. 400 lakhs. G Ltd. made further operating losses totalling Rs. 60 lakhs till 30th April 2018.

How should U Ltd. present the decision to discontinue the business of G Ltd. in its consolidated statement of comprehensive income as per Ind AS?

What are the provisions that the Company is required to make as per Ind AS 37?

(8 marks)

(C)

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

(a) Cash consideration of Rs. 15,00,000

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

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

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

Advise how the above transactions will be disclosed/presented in the statement of cash flows as per Ind AS 7. **(8 marks)**