



**J.K. SHAH<sup>®</sup>**  
**TEST SERIES**  
Evaluate Learn Succeed

**SUGGESTED SOLUTION**

**FINAL MAY 2019 EXAM**

**SUBJECT- FR**

**Test Code - FNJ 7106**

**BRANCH - () (Date :)**

**Head Office : Shraddha, 3<sup>rd</sup> Floor, Near Chinai College, Andheri (E), Mumbai – 69.**

**Tel : (022) 26836666**

**Answer 1:**

Breakdown of assets and liabilities acquired as part of the business combination, including deferred taxes and goodwill.

Item	Rs. In lakhs				
	Book value	Fair value	Tax base	Taxable (deductible) temporary difference	Deferred tax asset (liability) @ 30%
Cash	780	780 <sup>1)</sup>	780 <sup>1)</sup>	.	-
Receivables	5,200	5,200 <sup>1)</sup>	5,500 <sup>3)</sup>	(300)	90
Plant and equipment	7,000	8,000 <sup>2)</sup>	6,000 <sup>4)</sup>	2,000	(600)
Brands		4,300 <sup>4)</sup>	.5)	4,300	(1,290)
Goodwill (Balancing figure)		2,100 <sup>9)</sup>			
Deferred tax asset	360	3,60 <sup>7)</sup>			
<b>Total assets</b>		<b>20,740</b>			
Payables	(1,050)	(1,050) <sup>1)</sup>	(1,050) <sup>1)</sup>		
Borrowings	(4,900)	(4,900) <sup>1)</sup>	(4,900) <sup>1)</sup>	(900)	270
Employee Entitlement liabilities	(900)	(900) <sup>1)</sup>	.6)		
Deferred tax liability	(300)	(1,890) <sup>8)</sup>			
<b>Total liabilities</b>		<b>(8,740)</b>			
<b>Consideration paid</b>		<b>12,000</b>			

**(4 marks)****Notes**

- (1) This amount has been derived from Dorman Ltd.'s Balance Sheet as it is stated that 'unless otherwise stated, all items have a fair value and tax base equal to their carrying amounts in Dorman Ltd.'s Balance Sheet at the acquisition date'.
- (2) Stated fair value in the fact pattern (different to the carrying amount in Dorman Ltd.'s Balance Sheet at the acquisition date).
- (3) Because bad debts are only deductible when written off against the allowance account by Dorman Ltd. the tax base of the receivables is their gross value, i.e., (Rs. 5,200 + Rs. 300) lakhs allowance account.
- (4) Tax written down value of the plant and equipment as stated in the fact pattern.
- (5) As the brand name does not have a cost for tax purposes and no tax deduction is available in relation to it, its tax base is nil.
- (6) As the employee entitlement liabilities are only deductible for tax purposes when paid, their tax base is nil.
- (7) The aggregate deferred tax asset is Rs. 360 lakhs, comprised of Rs.90 lakhs in relation to the receivables and Rs.270 lakhs in relation to the employee entitlement liabilities.
- (8) The aggregate deferred tax liability is Rs. 1,890 lakhs calculated as follows:

Rs. In lakhs	DTL amount in Dorman Ltd.'s Balance Sheet	Deferred tax impact of fair value adjustments	Total DTL in Pharma Ltd's consolidated financial statements
Plant and equipment	300 $([7,000-6,000] \times 30\%)$	300 $([1,000 \times 30\%])$	600
Brand names	0	1,290 $(4,300 \times 30\%)$	1,290
TOTAL	300	1,590	1,890

(4 marks)

(9) Goodwill is effectively the 'balancing item' in the equation, applying the requirements of Ind AS 103, para 32. The consideration transferred is Rs. 12,000 lakhs and the net of the acquisition date amounts of the identifiable assets acquired and the liabilities assumed measured in accordance with Ind AS 103, including the deferred tax assets and liabilities arising, is Rs. 9,900 lakhs.

(2 marks)

Answer 2:  
(A)

All numbers in Rs. in 000.

The lease of the asset by A Ltd. to B Ltd. would be regarded as a finance lease because **the risks and rewards of ownership have been transferred to B Ltd.** Evidence of this includes the lease is for the whole of the life of the asset and B Ltd. being responsible for repairs and maintenance.

As per para 36 of Ind AS 17, since the lease is a finance lease and A Ltd. is the lessor, A Ltd. will recognise a financial asset ie. as **a receivable at an amount equal to the 'net investment in finance leases'**. The amount recognised will be the present value of the minimum lease payments which will be 20,197.39 ie.  $2,787 \times 7.247$ .

(3 marks)

The impact of the lease on the financial statements for the year ended 31<sup>st</sup> March, 2018 can best be seen by preparing a profile of the net investment in the lease for the first three years of the lease and shown below:

Year to 31 <sup>st</sup> March	Opening Balance	Finance income	Rental	Closing Balance
2017	20,197.39	1,615.79	(2,787)	19,026.18
2018	18,806	1,522.09	(2,787)	17,761.27
2019	17,301	1,420.90	(2,787)	16,395.17

During the year ended 31<sup>st</sup> March, 2018, A Ltd. will recognize income from finance leases of 1,522.09.

The net investment on 31<sup>st</sup> March, 2018 will be 17,761.27.

Of the closing net investment of 17,761.27, current asset will be shown for 2,787 and 14,974.27 as a non-current asset.

(2 marks)

(B)

The exchange gain or loss incurred by P on the trading balance should be recognised in profit or loss. Even if repayment was not due for three years (for example) or even longer, but if repayment is still planned, then the gain or loss should be recognised in profit or loss.

The amount lent by P should be regarded as part of its permanent funding to S. Thus, the exchange gain or loss incurred by P on the EURO 500 loan should be recognised in profit or loss in P's separate financial statements, but recognised in other comprehensive income and presented within equity in the consolidated financial statements. (5 marks)

**Answer 3:**

(A)

XYZ Ltd. would include the total revenue of Rs. 68,00,000 (Rs. 60,00,000 + Rs. 8,00,000) from ABC Ltd. received / receivable in the year ended 31<sup>st</sup> March 2018 within its revenue and show Rs. 18,00,000 within trade receivables at 31<sup>st</sup> March 2018.

**Mrs. P would be regarded as a related party of XYZ Ltd. because she is a close family member of one of the key management personnel of XYZ Ltd.**

From 1<sup>st</sup> June 2017, ABC Ltd. would also be regarded as a related party of XYZ Ltd. because from that date ABC Ltd. is an entity controlled by another related party.

Because ABC Ltd. is a related party with whom XYZ Ltd. has transactions, then XYZ Ltd. should disclose:

- The nature of the related party relationship.
- The revenue of Rs. 60,00,000 from ABC Ltd. since 1<sup>st</sup> June 2017.
- The outstanding balance of Rs. 18,00,000 at 31<sup>st</sup> March 2018.

In the current circumstances it may well be necessary for XYZ Ltd. to also disclose the favourable terms under which the transactions are carried out. (5 marks)

(B)

As per Ind AS 37, the conditions prescribed are:

- (a) there should be detailed formal plan of restructuring;
- (b) which should have raised valid expectations in the minds of those affected that the entity would carry out the restructuring by announcing the main features of its plans to restructure.

The board of directors did discuss and formalise a formal plan of winding up the operation in the above said state. This plan was communicated to the parties affected and created a valid expectation in their minds that X Cements Ltd. would go ahead with its plans to close down operations in that state. Thus, **there is a constructive obligation that needs to be provided at year-end.** (5 marks)

**Answer 4:**

**Ind AS 16 'Property, Plant and Equipment'** states that property, plant and equipment are tangible items that are held for use in the production or supply of goods or services, for rental to others, or for administrative purposes.

As per **Ind AS 40 'Investment property'**, investment property is a **property held to earn rentals** or for capital appreciation or both, rather than for use in the production or supply of goods or services or for administrative purposes or sale in the ordinary course of business.

Further, as per para 8 of Ind AS 40, **the building owned by the entity and leased out under one or more operating leases will be classified as investment property.**

Here top three floors have been leased out for 5 years with a non-cancellable period of 3 years. The useful life of the building is 50 years. The lease period is far less than the useful life of the building leased out. Further, the lease rentals of three years altogether do not recover

the fair value of the floors leased i.e. 15 crore x 30% = 4.50 crore. Hence the lease is an operating lease. Therefore, the 3 floors leased out as operating lease will be classified as investment property in the books of lessor i.e. UK Ltd.

However, for investment property, Ind AS 40 states that an entity shall adopt as its accounting policy the cost model to all of its investment property. Ind AS 40 also requires that an entity shall disclose the fair value of such investment property(ies). **(5 marks)**

(in crore)

	Total	PPE (70%)		Investment property (30%)
		Land (25%)	Building (75%)	
Cost	10	1.75	5.25	3
FV	15	2.625	7.875	4.5
Valuation mode		Cost	Cost	Cost (as per para 30 of Ind AS 40)
I followed				
Value recognized in the books		1.75	5.25	3
Less: Depreciation		Nil	(5.25/50) = 0.105 crore	(3/50) = 0.06
Carrying value as on 31 <sup>st</sup> March, 2018		1.75	5.145	2.94
Impairment loss		No impairment loss since fair value is more than the cost		

**(5 marks)**

**Answer 5:**

**(A)**

All figures are Rs. in '000.

On 31<sup>st</sup> March, 2018, A Ltd. will report a net pension liability in the statement of financial position. The amount of the liability will be 12,000 (68,000 – 56,000).

For the year ended 31<sup>st</sup> March, 2018, A Ltd. will report the current service cost as an operating cost in the statement of profit or loss. The amount reported will be 6,200. The same treatment applies to the past service cost of 1,500.

For the year ended 31<sup>st</sup> March, 2018, A Ltd. will report a finance cost in profit or loss based on the net pension liability at the start of the year of 8,000 (60,000 – 52,000). The amount of the finance cost will be 400 (8,000 x 5%).

The redundancy programme represents the partial settlement of the curtailment of a defined benefit obligation. The gain on settlement of 500 (8,000 – 7,500) will be reported in the statement of profit or loss.

Other movements in the net pension liability will be reported as remeasurement gains or losses in other comprehensive income. **(3 marks)**

For the year ended 31<sup>st</sup> March, 2018, the remeasurement loss will be 3,400 (Refer W. N.).

**Working Note:**

**Remeasurement of gain or loss**

	Rs. in '000
Liability at the start of the year (60,000 – 52,000)	8,000

Current service cost	6,200
Past service cost	1,500
Net finance cost	400
Gain on settlement	(500)
Contributions to plan	(7,000)
Remeasurement loss (balancing figure)	<u>3,400</u>
Liability at the end of the year (68,000 – 56,000)	<u>12,000</u>

(2 marks)

(B)

Computation of goodwill impairment

(3 marks)

	NCI at fair value	NCI at of net assets
	Rs. in '000	Rs. in '000
Cost of investment		
Share exchange (12,000 x 75% x 2/3 x Rs. 6.50)	39,000	39,000
Deferred consideration (7,150 / 1.10)	6,500	6,500
Contingent consideration	25,000	25,000
Non-controlling interest at date of acquisition:		
Fair value – 3000 x Rs. 6	18,000	
% of net assets – 68,000 (Refer W.N.) x 25%		17,000
Net assets on the acquisition date (Refer W.N.)	(68,000)	(68,000)
Goodwill on acquisition	20,500	19,500
Impairment @ 10%	2,050	1,950

**Working Note:**

(2 marks)

Net assets on the acquisition date	Rs. '000
Fair value at acquisition date	70,000
Deferred tax on fair value adjustments [20% x (70,000 – 60,000)]	<u>(2,000)</u>
	<u>68,000</u>