SUGGESTED SOLUTION

FINAL MAY 2019 EXAM

SUBJECT- FR

Test Code - FNJ 7109

BRANCH - () (Date :)

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Answer 1:

Identifying the acquirer **(1 marks)**

As a result of Entity A issuing 150 ordinary shares, Entity B's shareholders own 60 per cent of the issued shares of the combined entity (i.e., 150 of the 250 total issued shares). The remaining 40 per cent are owned by Entity A's shareholders. Thus, the transaction is determined to be a reverse acquisition in which Entity B is identified as the accounting acquirer while Entity A is the legal acquirer.

Calculating the fair value of the consideration transferred **(1 marks)**

If the business combination had taken the form of Entity B issuing additional ordinary shares to Entity A's shareholders in exchange for their ordinary shares in Entity A, Entity B would have had to issue 40 shares for the ratio of ownership interest in the combined entity to be the same. Entity B's shareholders would then own 60 of the 100 issued shares of Entity B — 60 per cent of the combined entity. As a result, the fair value of the consideration effectively transferred by Entity B and the group's interest in Entity A is 1,600 (40 shares with a fair value per share of 40).

The fair value of the consideration effectively transferred should be based on the most reliable measure. Here, the quoted market price of Entity A's shares provides a more reliable basis for measuring the consideration effectively transferred than the estimated fair value of the shares in Entity B, and the consideration is measured using the market price of Entity A's shares — 100 shares with a fair value per share of 16.

Measuring goodwill **(2 marks)**

Goodwill is measured as the excess of the fair value of the consideration effectively transferred (the group's interest in Entity A) over the net amount of Entity A's recognised identifiable assets and liabilities, as follows:

Consideration effectively transferred		1,600
Net recognised values of Entity A's identifiable assets and liabilities		
Current assets	500	
Non-current assets	1,500	
Current liabilities	(300)	
Non-current liabilities	(400)	(1,300)
Goodwill		300

Consolidated statement of financial position at September 30, 20X1 **(4 marks)**

The consolidated statement of financial position immediately after the business combination is:

Current assets [700 + 500]		1,200
Non-current assets [3,000 + 1,500]		4,500
Goodwill		300
	Total assets	6,000
Current liabilities [600 + 300]		900
Non-current liabilities [1,100 + 400]		1,500
	Total liabilities	2,400
Shareholders' equity		

Issued equity 250 ordinary shares [600 + 1,600]	2,200
Retained earnings	1,400
Total shareholders' equity	3,600
Total liabilities and shareholders' equity	6,000

The amount recognised as issued equity interests in the consolidated financial statements (2,200) is determined by adding the issued equity of the legal subsidiary immediately before the business combination (600) and the fair value of the consideration effectively transferred (1,600). However, the equity structure appearing in the consolidated financial statements (i.e., the number and type of equity interests issued) must reflect the equity structure of the legal parent, including the equity interests issued by the legal parent to effect the combination.

Earnings per share **(2 marks)**

Earnings per share for the annual period ended December 31, 20X1 is calculated as follows:

Number of shares deemed to be outstanding for the period from January 1, 20X1 to the acquisition date (i.e., the number of ordinary shares issued by Entity A (legal parent, accounting acquiree) in the reverse acquisition)	150
Number of shares outstanding from the acquisition date to December 31, 20X1	250
Weighted average number of ordinary shares outstanding [(150 × 9/12) + (250 × 3/12)]	175
Earnings per share [800 / 175]	4.57

Restated earnings per share for the annual period ended December 31, 20X0 is 4.00 [calculated as the earnings of Entity B of 600 divided by the number of ordinary shares Entity A issued in the reverse acquisition (150)].

Answer 2:
(A)

All numbers in Rs. in000.

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 x 7.247. **(3 marks)**

The impact of the lease on the financial statements for the year ended 31st 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 31st 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 31st March, 2018, A Ltd. will recognize income from finance leases of 1,522.09.

The net investment on 31st 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 31st March 2018 within its revenue and show Rs. 18,00,000 within trade receivables at 31st 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 1st 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 1st June 2017.
- The outstanding balance of Rs. 18,00,000 at 31st 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 that 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 ie. 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 model followed		Cost	Cost	Cost (as per para 30 of Ind AS 40)
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 31st 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 31st 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 31st 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 31st 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 31st 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)	3,400
Liability at the end of the year (68,000 – 56,000)	12,000

(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)]	(2,000)
	68,000