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SUBJECT : F.R.

Test Code – FNJ 7379

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NOTES : 1. NEW QUESTION SHOULD BE ON NEW PAGE

2. WORKING NOTES SHOULD FORM PART OF ANSWER

3. INTERNAL WORKING NOTES SHOULD ALSO BE EVALUATED.

ANSWER 1.

(i) As an only exception to the principle of classification or designation of assets as they exist at the acquisition date is that for lease contract and insurance contracts classification which will be based on the basis of the conditions existing at inception and not on acquisition date.

Therefore, H Ltd. would be required to retain the original lease classification of the lease arrangements and thereby recognise the lease arrangements as finance lease.

(1 MARK)

(ii) The requirements in Ind AS 37 'Provisions, Contingent Liabilities and Contingent Assets', do not apply in determining which contingent liabilities to recognise as of the acquisition date as per Ind AS 103 'Business Combination'. Instead, the acquirer shall recognise as of the acquisition date a contingent liability assumed in a business combination if it is a present obligation that arises from past events and its fair value can be measured reliably. Therefore, contrary to Ind AS 37, the acquirer recognises a contingent liability assumed in a business combination at the acquisition date even if it is not probable that an outflow of resources embodying economic benefits will be required to settle the obligation. Hence H Ltd. will recognize contingent liability of Rs. 2.5 cr.

Since S Ltd. has indemnified for Rs. 1 cr., H Ltd. shall recognise an indemnification asset at the same time for Rs. 1 cr.

As per the information given in the question, this indemnified asset is not taxable. Hence, its tax base will be equal to its carrying amount. No deferred tax will arise on it.

(2 MARKS)

(iii) As per Ind AS 103, non-current assets held for sale should be measured at fair value less cost to sell in accordance with Ind AS 105 'Non-current Assets Held for Sale and Discontinued Operations'. Therefore, its carrying value as per balance sheet has been considered in the calculation of net assets.

(1 MARK)

(iv) Any equity interest in S Ltd. held by H Ltd. immediately before obtaining control over S Ltd. is adjusted to acquisition-date fair value. Any resulting gain or loss is recognised in the profit or loss of H Ltd.

Calculation of purchase consideration as per Ind AS 103 **Rs.** in lakh

Investment in S Ltd.			
On 1st Nov. 2016	15%	[(12/100) x 395 x 15%]	7.11
On 1st Jan. 2017	45%		
Own equity given		10,000 x 12% x 45% x 1/2	270
Cash			50
Contingent consideration			22
			349.11

(2 MARKS)

(ii) Calculation of defer tax on assets and liabilities acquired as part of the business combination, including current tax and goodwill.

Item	**Rs. in crore**				
	Book value	**Fair value**	**Tax base**	**Taxable (deductible) temporary difference**	**Deferred tax assets (liability) @ 30%**
Property, plant and equipment	40	90	40	50	(15)
Intangible assets	20	30	20	10	(3)
Investments	100	350	100	250	(75)
Inventories	20	20	20	-	-
Trade receivables	20	20	20	-	-
Cash held in functional currency	4	4	4	-	-
Non-current asset held for sale	4	4	4	-	-
Indemnified asset	-	1	1	-	-
Borrowings	20	20	20	-	-
Trade payables	28	28	28	-	-
Provision for warranties	3	3	3	-	-
Current tax liabilities	4	4	4	-	-
Contingent liability		0.5	-	(0.5)	0.15
Deferred tax Liability					(92.85)

(3 MARKS)

(vi) Calculation of identifiable net assets acquired

	Rs. in crore	**Rs. in crore**
Property, plant and equipment	90	
Intangible assets	30	
Investments	350	
Inventories	20	
Trade receivables	20	
Cash held in functional currency	4	
Non-current asset held for sale	4	
Indemnified asset	1	
Total asset		519
Less: Borrowings	20	
Trade payables	28	

Provision for warranties	3	
Current tax liabilities	4	
Contingent liability (2 + 0.5)	2.50	
Deferred tax liability (W.N.2)	92.85	(150.35)
Net identifiable assets		368.65

(3 MARKS)

(a) Calculation of NCI by proportionate share of net assets

Net identifiable assets of S Ltd. on 1.1.2017 (Refer W.N.3) = 372.85

crore NCI on 1.1.2017 = 368.65 crore x 40% = 147.46 crore

Calculation of Goodwill as per Ind AS 103

Goodwill on 1.1.2017 = Purchase consideration + NCI – Net assets

= 349.11 + 147.46 – 368.65

= 127.92 crore

(2 MARKS)

(b) As per para 45 of Ind AS 103 'Business Combination', if the initial accounting for a business combination is incomplete by the end of the reporting period in which the combination occurs, the acquirer shall report in its financial statements provisional amounts for the items for which the accounting is incomplete.

During the measurement period, the acquirer shall retrospectively adjust the provisional amounts recognised at the acquisition date to reflect new information obtained about facts and circumstances that existed as of the acquisition date and, if known, would have affected the measurement of the amounts recognised as of that date.

During the measurement period, the acquirer shall also recognise additional assets or liabilities if new information is obtained about facts and circumstances that existed as of the acquisition date and, if known, would have resulted in the recognition of those assets and liabilities as of that date.

The measurement period ends as soon as the acquirer receives the information it was seeking about facts and circumstances that existed as of the acquisition date or learns that more information is not obtainable. However, the measurement period shall not exceed one year from the acquisition date.

Further, as per para 46 of Ind AS 103, the measurement period is the period after the acquisition date during which the acquirer may adjust the provisional amounts recognised for a business combination. The measurement period provides the acquirer with a reasonable time to obtain the information necessary to identify and measure the fo llowing as of the acquisition date in accordance with the requirements of this Ind AS:

(a) the identifiable assets acquired, liabilities assumed and any non-controlling interest in the acquiree;

(b) .....

(c) ......; and

(d) the resulting goodwill or gain on a bargain purchase.

Para 48 states that the acquirer recognises an increase (decrease) in the provisional amount recognised for an identifiable asset (liability) by means of a decrease (increase) in goodwill.

Para 49 states that during the measurement period, the acquirer shall recognise adjustments to the provisional amounts as if the accounting for the business combination had been completed at the acquisition date.

Para 50 states that after the measurement period ends, the acquirer shall revise the accounting for a business combination only to correct an error in accordance with Ind AS 8 'Accounting Policies, Changes in Accounting Estimates and Errors'.

On 31st December, 2017, H Ltd. has established that it has obtained all the information necessary for the accounting of the business combination and the more information is not obtainable. Therefore, the measurement period for acquisition of S Ltd. ends on 31 st December, 2017.

On 31st May, 2017 (ie within the measurement period), H Ltd. learned that certain customer relationships existing as on 1st January, 2017 which met the recognition criteria of an intangible asset as on that date were not considered during the accounting of business combination for the year ended 31st March, 2017. Therefore, H Ltd. shall account for the acquisition date fair value of customer relations existing on 1st January, 2017 as an identifiable intangible asset. The corresponding adjustment shall be made in the amount of goodwill.

Accordingly, the amount of goodwill will be changed due to identification of new asset from retrospective date for changes in fair value of assets and liabilities earlier recognised on provisional amount (subject to meeting the condition above for measurement period). NCI changes would impact the consolidated retained earnings (parent's share). Also NCI will be increased or decreased based on the profit during the post-acquisition period.

Journal entry

Customer Relationship	Dr.	3.5 crore	
To NCI			1.4 crore
To Goodwill			2.1 crore

However, the increase in the value of customer relations after the acquisition date shall not be accounted by H Ltd., as the customer relations developed after 1st January, 2017 represents internally generated intangible assets which are not eligible for recognition on the balance sheet.

(4 MARKS)

(c) Since the contingent considerations payable by H Ltd is not classified as equity and is within the scope of Ind AS 109 'Financial Instruments', the changes in the fair value shall be recognised in profit or loss. Change in Fair value of contingent consideration (23 -22) Rs. 1 crore will be recognized in the Statement of Profit and Loss.

(2 MARKS)

ANSWER 2(A).

Considering facts of the case, Seller-lessee and buyer-lessor account for the transaction as a sale and leaseback.

Firstly, since the consideration for the sale of the building is not at fair value, Seller-lessee and Buyer - lessor make adjustments to measure the sale proceeds at fair value. Thus, the amount of the excess sale price of Rs. 3,00,000 (as calculated below) is recognised as additional financing provided by Buyer-lessor to Seller-lessee.

Sale Price:	30,00,000
Less: Fair Value (at the date of sale):	(27,00,000)
Additional financing provided by Buyer-lessor to Seller-lessee	**3,00,000**

Next step would be to calculate the present value of the annual payments which amounts to Rs. 14,94,000 (calculated considering 20 payments of Rs. 2,00,000 each, discounted at 12% p.a.) of which Rs. 3,00,000 relates to the additional financing (as calculated above) and balance Rs. 11,94,000 relates to the lease — corresponding to 20 annual payments of Rs. 40,164 and Rs. 1,59,836, respectively (refer calculations below).

Proportion of annual lease payments:

Present value of lease payments (as calculated above)	(A)	14,94,000
Additional financing provided (as calculated above)	(B)	3,00,000
Relating to the Additional financing provided	(C) = (E x B / A)	40,160
Relating to the Lease	(D) = (E – C)	1,59,840
Annual payments (at the end of each year)	(E)	2,00,000

(6 MARKS)

<u>**Seller-Lessee:**</u>

At the commencement date, Seller-lessee measures the ROU asset arising from the leaseback of the building at the proportion of the previous carrying amount of the building that relates to the right-of-use retained by Seller-lessee, calculated as follows:

Carrying Amount	(A)	15,00,000
Fair Value (at the date of sale)	(B)	27,00,000
Discounted lease payments for the 20-year ROU asset	(C)	11,94,000
ROU Asset	**[(A / B) x C]**	**6,63,333**

Seller-lessee recognises only the amount of the gain that relates to the rights transferred to Buyer- lessor, calculated as follows:

Fair Value (at the date of sale) (A)	27,00,000
Carrying Amount (B)	15,00,000
Discounted lease payments for the 20-year ROU asset (C)	11,94,000
Gain on sale of building (D) = (A - B)	**12,00,000**
Relating to the right to use the building retained by Seller-lessee (E) = [(D / A) x C]	5,30,667
Relating to the rights transferred to Buyer-lessor (D - E)	6,69,333

At the commencement date, Seller-lessee accounts for the transaction, as follows:

Cash	Dr.	30,00,000	
ROU Asset	Dr.	6,63,333	
To Building			15,00,000
To Financial Liability			14,94,000
To Gain on rights transferred			6,69,333

Buyer-Lessor:

At the commencement date, Buyer-lessor accounts for the transaction, as follows:

Building	Dr.	27,00,000	
Financial Asset (20 payments of Rs. 40,160 discounted @ 12% p.a.) (approx.)	Dr.	3,00,000	
To Cash			30,00,000

After the commencement date, Buyer-lessor accounts for the lease by treating Rs. 1,59,840 of the annual payments of Rs. 2,00,000 as lease payments. The remaining Rs. 40,160 of annual payments received from Seller-lessee are accounted for as:

(a) payments received to settle the financial asset of Rs. 3,00,000 ***AND***

(b) interest revenue.

(6 MARKS)

ANSWER 2(B).

The above treatment needs to be examined in the light of the provisions given in Ind AS 10 'Events after the Reporting Period' and Ind AS 2 'Inventories'.

Para 3 of Ind AS 10 'Events after the Reporting Period' defines "Events after the reporting period are those events, favourable and unfavourable, that occur between the end of the reporting period and the date when the financial statements are approved by the Board of Directors in case of a company, and, by the corresponding approving authority in case of any other entity for issue. Two types of events can be identified:

(a) those that provide evidence of conditions that existed at the end of the reporting period (adjusting events after the reporting period); and

(b) those that are indicative of conditions that arose after the reporting period (non adjusting events after the reporting period).

Further, paragraph 10 of Ind AS 10 states that:

"An entity shall not adjust the amounts recognised in its financial statements to reflect non-adjusting events after the reporting period".

Further, paragraph 6 of Ind AS 2 defines:

"Net realisable value is the estimated selling price in the ordinary course of business less the estimated costs of completion and the estimated costs necessary to make the sale".

Further, paragraph 9 of Ind AS 2 states that:

"Inventories shall be measured at the lower of cost and net realisable value".

Accountant of Jupiter Ltd. has re-measured the inventories after adjusting the event in its financial statement which is not correct and nor in accordance with provision of Ind AS 2 and Ind AS 10.

Accordingly, the event causing the damage to the inventory occurred after the reporting date and as per the principles laid down under Ind AS 10 'Events After the Reporting Date' is a non-adjusting event as it does not affect conditions at the reporting date. Non-adjusting events are not recognised in the financial statements, but are disclosed where their effect is material.

Therefore, as per the provisions of Ind AS 2 and Ind AS 10, the consignment of inventories shall be recorded in the Balance Sheet at a value of Rs. 8 lakhs calculated below:

Rs.' lakhs

Cost	8.00
Net realisable value	9.60
Inventories (lower of cost and net realisable value)	8.00

(8 MARKS)

ANSWER 3(A).

Journal Entries

Purchase of Machinery on credit basis on 30th January 20X1:

		Rs.	Rs.
Machinery A/c (5,000 x $ 60)	Dr.	3,00,000	
To Creditors			3,00,000
(Initial transaction will be recorded at exchange rate on the date of transaction)			

Exchange difference arising on translating monetary item on 31st March 20X1:

		Rs.	Rs.
Machinery A/c [(5,500 x $ 65) – (5,000 x $ 60)]	Dr.	57,500	
To Profit & loss a/c (Exchange Profit & Loss)			57,500
Profit & Loss A/c [(5,000 x $ 65) – (5,000 x $ 60)]	Dr.	25,000	
To Creditors			25,000

Exchange difference arising on translating monetary item and settlement of creditors on 31st March 20X2:

		Rs.	Rs.
Creditors A/c (5,000 x $65)	Dr.	3,25,000	
Profit & loss A/c [(5,000 x ($ 67 -$ 65)]	Dr.	10,000	
To Bank A/c			3,35,000
Machinery A/c [(5,500*($ 67-$ 65))	Dr.	11,000	
To Profit & loss A/c			11,000

(6 MARKS)

OR

ANSWER 3(A).

This is the case of Revenue recognised at a single point in time with multiple payments. As per the guidance given in Appendix B to Ind AS 21:

A Ltd. will recognise a non-monetary contract liability amounting Rs. 1,440 million, by translating USD 20 million at the exchange rate on 1st January, 2018 ie Rs. 72 per USD.

A Ltd. will recognise revenue at 31st March, 2018 (that is, the date on which it transfers the goods to the customer).

A Ltd. determines that the date of the transaction for the revenue relating to the advance consideration of USD 20 million is 1st January, 2018. Applying paragraph 22 of Ind AS 21, A Ltd. determines that the date of the transaction for the remainder of the revenue as 31st March, 2018.

On 31st March, 2018, A Ltd. will:

- derecognise the non-monetary contract liability of USD 20 million and recognise USD 20 million of revenue using the exchange rate as at 1st January, 2018 ie Rs. 72 per USD; and
- recognise revenue and a receivable for the remaining USD 30 million, using the exchange rate on 31st March, 2018 ie Rs. 75 per USD.
- The receivable of USD 30 million is a monetary item, so it should be translated using the closing rate until the receivable is settled.

(6 MARKS)

ANSWER 3(B).

Assessment of the arrangement using the definition of derivative included under Ind AS 109.

Derivative is a financial instrument or other contract within the scope of this Standard with all three of the following **characteristics:**

(a) its value changes in response to the change in foreign exchange rate (emphasis laid)

(b) it requires no initial net investment or an initial net investment is smaller than would be required for other types of contracts with similar response to changes in market factors.

(c) it is settled at a future date.

Upon evaluation of contract in question, on the basis of the definition of derivative, it is noted that the contract meets the definition of a derivative as follows:

(a) the value of the contract to purchase USD at a fixed price changes in response to changes in foreign exchange rate.

(b) the initial amount paid to enter into the contract is zero. A contract which would give the holder a similar response to foreign exchange rate changes would have required an investment of USD 40,000 on inception.

(c) the contract is settled in future

The derivative is a forward exchange contract.

As per Ind AS 109, derivatives are measured at fair value upon initial recognition and are subsequently measured at fair value through profit and loss.

(3 MARKS)

Accounting in each Quarter

(i) Accounting on 1st January 2017

As there was no consideration paid and without evidence to the contrary the fair value of the contract on the date of inception is considered to be zero. Accordingly, no accounting entries shall be recorded on the date of entering into the contract.

(ii) Accounting on 31st March 2017

Particulars	**Dr. (Rs.)**	**Cr. (Rs.)**
Profit and loss A/c Dr.	50,000	
To Derivative financial liability		50,000
(Being mark to market loss on forward contract recorded)		

(iii) Accounting on 30th June 2017

Particulars	**Dr. (Rs.)**	**Cr. (Rs.)**
Derivative financial liability A/c Dr.	20,000	
To Profit and Loss A/c		20,000
(Being partial reversal of mark to market loss on forward contract recorded)		

(iv) Accounting on 30th September 2017

Particulars	**Dr. (Rs.)**	**Cr. (Rs.)**
Derivative financial liability A/c Dr.	30,000	
Derivative financial asset A/c Dr.	24,000	
To Profit and Loss A/c		54,000
(Being gain on mark to market of forward contract booked as derivative financial asset and reversal of derivative financial liability)		

(v) **Accounting on 31st December 2017**

The settlement of the derivative forward contract by actual purchase of USD 40,000

Particulars	Dr. (Rs.)	Cr. (Rs.)
Cash (USD Account) (USD 40,000 x Rs.62)Dr.	24,80,000	
Profit and loss A/c Dr.	1,44,000	
To Cash (USD 40,000 x Rs. 65)		26,00,000
To Derivative financial asset A/c		24,000
(Being loss on settlement of forward contract booked on actual purchase of USD)		

(5 MARKS)

ANSWER 3(C).

Ind AS 38 'Intangible Assets' requires an intangible asset to be recognised if, and only if, certain criteria are met. Regulatory approval on 1 June 20X5 was the last criterion to be met, the other criteria have been met as follows:

- Intention to complete the asset is apparent as it is a major project with full support from board
- Finance is available as resources are focused on project
- Costs can be reliably measured
- Benefits are expected to exceed costs – (in 2 years)

Amount of Rs. 15,00,000 (Rs. 18,00,000 x 10/12) should be capitalised in the Balance sheet of year ending 20X5-20X6 representing expenditure since 1 June 20X5.

The expenditure incurred prior to 1 June 20X5 which is Rs. 3,00,000 (2/12 x Rs. 18,00,000) should be recognised as an expense, retrospective recognition of expense as an asset is not allowed.

Ind AS 36 'Impairment of assets' requires an intangible asset not yet available for use to be tested for impairment annually.

Cash flow of Rs. 12,00,000 in perpetuity would clearly have a present value in excess of Rs. 12,00,000 and hence there would be no impairment. However, the research director is technically qualified, so impairment tests should be based on her estimate of a four-year remaining life and so present value of the future cost savings of Rs. 9,60,000 should be considered in that case Rs. 9,60,000 is greater than the offer received (fair value less costs to sell) of Rs. 7,80,000 and so Rs. 9,60,000 should be used as the recoverable amount.

So, the carrying amount should be consequently reduced to Rs. 9,60,000.

Calculation of Impairment loss:

Particulars	**Amount Rs.**
Carrying amount (Restated)	15,00,000
Less: Recoverable amount	9,60,000
Impairment loss	5,40,000

Impairment loss of Rs. 5,40,000 is to be recognised in the profit and loss for the year 20X5-20X6. Necessary adjusting entry to correct books of account will be:

	Rs.	Rs.
Operating expenses- Development expenditure Dr. Operating expenses–Impairment loss of intangible assets Dr. To Intangible assets – Development expenditure	3,00,000 5,40,000	 8,40,000

(6 MARKS)

ANSWER 4(A).

Ind AS 37 "Provisions, Contingent Liabilities and Contingent Assets" defines an onerous contract as "a contract in which the unavoidable costs of meeting the obligations under the contract exceed the economic benefits expected to be received under it".

Paragraph 68 of Ind AS 37 states that "the unavoidable costs under a contract reflect the least net cost of exiting from the contract, which is the lower of the cost of fulfilling it and any compensation or penalties arising from failure to fulfill it".

In the instant case, cost of fulfilling the contract is Rs. 0.5 million (Rs. 2.5 million – Rs. 2 million) and cost of exiting from the contract by paying penalty is Rs. 0.25 million.

In accordance with the above reproduced paragraph, it is an onerous contract as cost of meeting the contract exceeds the economic benefits.

Therefore, the provision should be recognised at the best estimate of the unavoidable cost, which is lower of the cost of fulfilling it and any compensation or penalties arising from failure to fulfill it, i.e., at Rs. 0.25 million (lower of Rs. 0.25 million and Rs. 0.5 million).

(5 MARKS)

ANSWER 4(B).

As required by paragraph B53 of the Ind AS 102, over the two-year vesting period, the subsidiary measures the services received from the employees in accordance, the requirements applicable to equity-settled share-based payment transactions as given in paragraph 43B. Thus, the subsidiary measures the services received from the employees on the basis of the fair value of the share options at grant date. An increase in equity is recognised as a contribution from the parent in the separate or individual financial statements of the subsidiary.

The journal entries recorded by the subsidiary for each of the two years are as follows:

Year 1	Rs.	Rs.
Remuneration expense Dr. (200 x 100 employees x Rs. 30 x 80% x ½)	2,40,000	
To Equity (Contribution from the parent)		2,40,000
Year 2		
Remuneration expense Dr. [(200 x 81 employees x Rs. 30) – 2,40,000]	2,46,000	
To Equity (Contribution from the parent)		2,46,000

(5 MARKS)

ANSWER 4(C).

Computation of Deferred Tax Liability

(i) MAT credit as on 31st December of Rs. 9.75 crore will be presented in the Balance Sheet as Deferred tax asset. DTA in the current year will be Rs. 1.25 crore (Rs. 9.75 crore – Rs. 8.50 crore)

(1 MARK)

(ii) (a) In case defer tax is created only on account of depreciation

	Carrying value without revaluation	**Value as Per tax records**	**Tax base**	**Taxable**	**Total Deferred tax liability/ (asset) @ 20%**	**Credit to P&L during the year**
A	**b**	**c**	**d**	**E= b-d**	**F = e x 20%**	**g**
31st March, 2016	22 crore	22 crore	22 crore	nil	nil	nil
Less: Depreciation for the year 2016- 17	(2 crore)	(1.25 crore)				
Carrying value as on 31st March, 2017	20 crore	20.75 crore	20.75 crore	(0.75 crore)	DTA (0.15 crore)	DTA (0.15 crore)

(3 MARKS)

(b) Computation of tax effect taking into account the revalued figures and adjusting impact of tax effect on account of difference in depreciation

S. No.		**Carrying value after revaluation**	**Value as per tax records**	**Tax base**	**Taxable / (deductible) temporary difference**	**Total Deferred tax liability/ (asset) @ 20%**	**Credit to P&L during the year**	**Charged to OCI during the year**
	a	b	c	d	E= b-d	F = e x 20%	g	h
I	31st March, 2016	40 crore	22 crore	22 crore	18 crore	DTL 3.6 crore	-	DTL 3.6 crore
IV	Revalued again on 31.3.2017 (It is assumed that revaluation has been done after taking into consideration the impact of depreciation for the current year)	45 crore	20.75 crore (22- 1.25)	20.75 crore	24.25 crore	DTL 4.85 crore	DTA (0.15 crore) (Refer table (a) above)	DTL 5 crore (Refer Note below) [5 DTL (B/F) – 0.15 DTA = 4.85 DTL]
V	Additional DTL/DTA required during the year (IV-I)					DTL 1.25 crore	DTA (0.15 crore) (Refer table (a))	DTL (1.40 crore) (Refer Note below)

(4 MARKS)

Note:

As per para 65 of Ind AS 12, when an asset is revalued for tax purposes and that revaluation is related to an accounting revaluation of an earlier period, or to one that is expected to be carried out in a future period, the tax effects on account of revaluation of asset and the adjustment of the tax base are recognised in other comprehensive income in the periods in which they occur.

Here, it is important to understand that only the tax effects on account of revaluation of asset and the adjustment of the tax base are recognised in other comprehensive income. However, tax effects on account of depreciation of asset and the adjustment of the tax base are recognized in profit and loss.

Accordingly, first of all the tax effect has been calculated assuming that there is no revaluation (Refer Table (a) above) [Since the information for the carrying value before revaluation has not been mentioned, it is assumed to be equal to the carrying amount as per the tax records]. Later the DTA arrived due to difference in depreciation is adjusted with the DTL created due to revaluation. DTA of Rs. 0.15 crore on account of depreciation will be charged to Profit and Loss and DTL of Rs. 1.40 crore will be charged to OCI. Net effect in the year 31.3.2017 will be DTL 1.25 crore (DTL 1.4 crore – DTA 0.15 crore) [Refer Table (b) above.]

(2 MARKS)

ANSWER 5(A).

This is a compound financial instrument with two components – liability representing present value of future cash outflows and balance represents equity component.

a. Computation of Liability & Equity Component

Date	Particulars	Cash Flow	Discount Factor	Net present Value
01-Apr-20X1		0	1	0.00
31-Mar-20X2	Dividend	150,000	0.869565	130,434.75
31-Mar-20X3	Dividend	150,000	0.756144	113,421.6
31-Mar-20X4	Dividend	150,000	0.657516	98,627.4
31-Mar-20X5	Dividend	150,000	0.571753	85,762.95
31-Mar-20X6	Dividend	150,000	0.497177	74,576.55
Total Liability Component				502,823.25
Total Proceeds				1,500,000.00
Total Equity Component (Bal fig)				997,176.75

(2 MARKS)

b. Allocation of transaction costs

Particulars	Amount	Allocation	Net Amount
Liability Component	502,823	10,056	492,767
Equity Component	997,177	19,944	977,233
Total Proceeds	1,500,000	30,000	1,470,000

(1 MARK)

c. Accounting for liability at amortised cost:

- Initial accounting = Present value of cash outflows less transaction costs
- Subsequent accounting = At amortised cost, i.e., initial fair value adjusted for interest and repayments of the liability.

Assume the effective interest rate is 15.86%

	Opening Financial Liability A	Interest B	Cash Flow C	Closing Financial Liability A+B-C
01-Apr-20X1	492,767	-	-	4,92,767
31-Mar-20X2	492,767	78,153	150,000	4,20,920
31-Mar-20X3	420,920	66,758	150,000	3,37,678
31-Mar-20X4	337,678	53,556	150,000	2,41,234
31-Mar-20X5	241,234	38,260	150,000	1,29,494
31-Mar-20X6	129,494	20,506	150,000	-

(3 MARKS)

d. Journal Entries to be recorded for entire term of arrangement are as follows:

Date	Particulars	Debit	Credit
01-Apr-20X1	Bank A/c Dr.	1,470,000	
	To Preference Shares A/c		492,767
	To Equity Component of Preference shares A/c		977,233
	(Being compulsorily convertible preference shares issued. The same are divided into equity component and liability component as per the calculation)		
31-Mar-20X2	Preference shares A/c Dr.	150,000	
	To Bank A/c		150,000
	(Being Dividend at the coupon rate of 10% paid to the shareholders)		
31-Mar-20X2	Finance cost A/c Dr.	78,153	
	To Preference Shares A/c		78,153
	(Being interest as per EIR method recorded)		
31-Mar-20X3	Preference shares A/c Dr.	150,000	
	To Bank A/c		150,000
	(Being Dividend at the coupon rate of 10% paid to the shareholders)		
31-Mar-20X3	Finance cost A/c Dr.	66,758	
	To Preference Shares A/c		66,758
	(Being interest as per EIR method recorded)		
31-Mar-20X4	Preference shares A/c Dr.	150,000	

	To Bank A/c (Being Dividend at the coupon rate of 10% paid to the shareholders)		150,000
31-Mar-20X4	Finance cost A/c Dr. To Preference Shares A/c (Being interest as per EIR method recorded)	53,556	53,556
31-Mar-20X5	Preference shares A/c Dr. To Bank A/c (Being Dividend at the coupon rate of 10% paid to the shareholders)	150,000	150,000
31-Mar-20X5	Finance cost A/c Dr. To Preference Shares A/c (Being interest as per EIR method recorded)	38,260	38,260
31-Mar-20X6	Preference shares A/c Dr. To Bank A/c (Being Dividend at the coupon rate of 10% paid to the shareholders)	150,000	150,000
31-Mar-20X6	Finance cost A/c Dr. To Preference Shares A/c (Being interest as per EIR method recorded)	20,506	20,506
31-Mar-20X6	Equity Component of Preference shares A/c Dr. To Equity Share Capital A/c To Securities Premium A/c (Being Preference shares converted in equity shares and remaining equity component is recognised as securities premium)	977,233	50,000 927,233

(6 MARKS)

ANSWER 5(B).

Case A—Variable consideration allocated entirely to one performance obligation

To allocate the transaction price, the entity considers the criteria in paragraph 85 and concludes that the variable consideration (ie the sales-based royalties) should be allocated entirely to Licence B. The entity concludes that the criteria are met for the following reasons:

(a) the variable payment relates specifically to an outcome from the performance obligation to transfer Licence B (ie the customer's subsequent sales of products that use Licence B).

(b) allocating the expected royalty amounts of Rs. 2,000,000 entirely to Licence B is consistent with the allocation objective in paragraph 73 of Ind AS 115. This is because the entity's estimate of the amount of sales-based royalties (Rs. 2,000,000) approximates the stand- alone selling price of Licence B and the fixed amount of Rs. 1,600,000 approximates the stand-alone selling price of Licence A. The entity allocates Rs. 1,600,000 to Licence A. This is because, based on an assessment of the facts and circumstances relating to both licences, allocating to Licence B some of the fixed consideration in addition to all of the variable consideration would not meet the allocation objective in paragraph 73 of Ind AS 115.

The entity transfers Licence B at inception of the contract and transfers Licence A one month later. Upon the transfer of Licence B, the entity does not recognise revenue because the consideration allocated to Licence B is in the form of a sales-based royalty. Therefore, the entity recognises revenue for the sales-based royalty when those subsequent sales occur.

When Licence A is transferred, the entity recognises as revenue the Rs. 1,600,000 allocated to Licence A.

(4 MARKS)

Case B—Variable consideration allocated on the basis of stand-alone selling prices

To allocate the transaction price, the entity applies the criteria in paragraph 85 of Ind AS 115 to determine whether to allocate the variable consideration (ie the sales-based royalties) entirely to Licence B.

In applying the criteria, the entity concludes that even though the variable payments relate specifically to an outcome from the performance obligation to transfer Licence B (ie the customer's subsequent sales of products that use Licence B), allocating the variable consideration entirely to Licence B would be inconsistent with the principle for allocating the transaction price. Allocating Rs. 600,000 to Licence A and Rs. 3,000,000 to Licence B does not reflect a reasonable allocation of the transaction price on the basis of the stand-alone selling prices of Licences A and B of Rs. 1,600,000 and Rs. 2,000,000, respectively. Consequently, the entity applies the general allocation requirements of Ind AS 115.

The entity allocates the transaction price of Rs. 600,000 to Licences A and B on the basis of relative stand-alone selling prices of Rs. 1,600,000 and Rs. 2,000,000, respectively. The entity also allocates the consideration related to the sales-based royalty on a relative stand-alone selling price basis. However, when an entity licenses intellectual property in which the consideration is in the form of a sales-based royalty, the entity cannot recognise revenue until the later of the following events: the subsequent sales occur or the performance obligation is satisfied (or partially satisfied).

Licence B is transferred to the customer at the inception of the contract and Licence A is transferred three months later. When Licence B is transferred, the entity recognises as revenue Rs. 333,333 [(Rs. 2,000,000 ÷ Rs. 3,600,000) × Rs. 600,000] allocated to Licence B. When Licence A is transferred, the entity recognises as revenue Rs. 266,667 [(Rs. 1,600,000 ÷ Rs. 3,600,000) × Rs. 600,000] allocated to Licence A.

In the first month, the royalty due from the customer's first month of sales is Rs. 400,000. Consequently, the entity recognises as revenue Rs. 222,222 (Rs. 2,000,000 ÷ Rs. 3,600,000 × Rs. 400,000) allocated to Licence B (which has been transferred to the customer and is therefore a satisfied performance obligation). The entity recognises a contract liability for the Rs. 177,778 (Rs. 1,600,000 ÷ Rs. 3,600,000 × Rs. 400,000) allocated to Licence A. This is because although the subsequent sale by the entity's customer has occurred, the performance obligation to which the royalty has been allocated has not been satisfied.

(4 MARKS)

ANSWER 6(A).

A. As per section 135 of the Companies Act 2013

Every company having either

- net worth of Rs. 500 crore or more, or
- turnover of Rs. 1,000 crore or more or
- a net profit of Rs. 5 crore or more

<u>during any financial year</u> shall constitute a Corporate Social Responsibility (CSR) Committee of the Board consisting of three or more directors (including at least one independent director).

B. Role of Corporate Social Responsibility (CSR) Committee

The CSR Committee shall—

(a) formulate and recommend to Board-

  a. a CSR Policy indicating the activities to be undertaken by the company as specified in Schedule VII;

  b. the amount of expenditure to be incurred on the above activities and

(b) monitor the CSR Policy of the company from time to time.

C. Role of Board

Board shall disclose-

(a) The composition of CSR Committee in its report

(b) Approve the recommended CSR Policy for the company

(c) Disclose the contents of such Policy in its report and place it on the company's website

(d) Ensure that the activities included in CSR Policy of the company are duly executed by the company

(e) Ensure that the **company spends, in every financial year, at least two percent** of the **average net profits** of the company made **during the three immediately preceding financial years** by giving preference to the local area and areas around it where it operates

(f) In case the company fails to spend such amount, the Board shall specify the reasons for not spending the amount.

D. In the given scenario

The MCA has clarified that 'any financial year' referred to under sub-section (1) of section 135 of the Act read with Rule 3(2) of Companies CSR Rule, 2014, implies 'any of the three preceding financial years'.

A company which meets the 'net worth', 'turnover' or 'net profits' criteria in any of the preceding three financial years, but which does not meet the criteria in the relevant financial year, is still required to constitute a CSR Committee and comply with provisions of sections 135 of the Companies Act, 2013.

As per the criteria to constitute CSR committee -

1) <u>Net worth greater than or equal to Rs. 500 Crore:</u> This criterion is not satisfied.
2) <u>Sales greater than or equal to Rs. 1000 Crore:</u> This criterion is not satisfied.

3) Net Profit greater than or equal to Rs. 5 Crore: This criterion is satisfied in financial year ended March 31, 2017 when the net profit was Rs. 8 crore.

Hence, the XYZ Ltd. is required to form a CSR committee.

(8 MARKS)

ANSWER 6(B).

Subsidiary's earnings per share

Basic EPS	Rs. 5.00 calculated:	Rs. 5,400 (a) – Rs.400 (b) 1,000 (c)
Diluted EPS	Rs. 3.66 calculated:	Rs. 5,400 (d) (1,000 + 75 (e) + 400(f))

Notes:

(a) Subsidiary's profit attributable to ordinary equity holders.

(b) Dividends paid by subsidiary on convertible preference shares.

(c) Subsidiary's ordinary shares outstanding.

(d) Subsidiary's profit attributable to ordinary equity holders (Rs. 5,000) increased by Rs. 400 preference dividends for the purpose of calculating diluted earnings per share.

(e) Incremental shares from warrants, calculated: [(Rs. 20 – Rs. 10) ÷ Rs. 20] × 150.

(f) Subsidiary's ordinary shares assumed outstanding from conversion of convertible preference shares, calculated: 400 convertible preference shares × conversion factor of 1.

Consolidated earnings per share

Basic EPS Rs. 1.63 calculated: $$\frac{\text{Rs. } 12{,}000(\text{a}) + \text{Rs. } 4{,}300(\text{b})}{10{,}000(\text{c})}$$

Diluted EPS Rs. 1.61 calculated: $$\frac{\text{Rs. } 12{,}000 + \text{Rs. } 2{,}928(\text{d}) + \text{Rs. } 55(\text{e}) + \text{Rs. } 1{,}098(\text{f})}{10{,}000}$$

(a) Parent's profit attributable to ordinary equity holders of the parent entity.

(b) Portion of subsidiary's profit to be included in consolidated basic earnings per share, calculated: (800 × Rs. 5.00) + (300 × Re 1.00).

(c) Parent's ordinary shares outstanding.

(d) Parent's proportionate interest in subsidiary's earnings attributable to ordinary shares, calculated: (800 ÷ 1,000) × (1,000 shares × Rs. 3.66 per share).

(e) Parent's proportionate interest in subsidiary's earnings attributable to warrants, calculated: (30 ÷ 150) × (75 incremental shares × Rs. 3.66 per share).

(f) Parent's proportionate interest in subsidiary's earnings attributable to convertible preference shares, calculated: (300 ÷ 400) × (400 shares from conversion × Rs. 3.66 per share).

(8 MARKS)

ANSWER 6(C).

The entity should use First-In, First-Out (FIFO) method for its Ind AS 108 disclosures, even though it uses the weighted average cost formula for measuring inventories for inclusion in its financial statements. Where chief operating decision maker uses only one measure of segment asset, same measure should be used to report segment information. Accordingly, in the given case, the method used in preparing the financial information for the chief operating decision maker should be used for reporting under Ind AS 108.

However, reconciliation between the segment results and results as per financial statements needs to be given by the entity in its segment report.

(4 MARKS)