J.K. SHAH TEST SERIES
Evaluate Learn Succeed

CA FINAL
Test Code – JKN-GFR-21
(Date:)

(Marks - 100)

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

Rainbow Limited is a large manufacturing company that has already adopted Ind AS. during the financial year 2017-18. The company is in the process of preparing its financial statements as per Ind AS for the financial year 2019-20. Some new developments have taken place during the year and the company is keen that the appropriate accounting treatment and disclosures under Ind AS are determined and highlighted to the Board of Directors. Rainbow Limited's CFO has sought your assistance and shared the following details with you.

Rainbow Limited is an Indian entity whose functional currency is INR. It has taken a plant on lease from Entity Y for 5 years to use in its manufacturing process
for which it has to pay annual rentals in arrears of USD 10,000 every year.
On the commencement date, exchange rate was USD = INR 68. The average
rate for Year 1 was 69 and at the end of year 1, (31/03/2020) the exchange rate was 70. The incremental borrowing rate of Entity X on commencement of the lease for a USD borrowing was 5% p.a.

Four years ago, Rainbow Limited had acquired a commercial property for Rs.40 crores and immediately leased out the same to Turquoise Limited on an operating lease basis. The annual rental as per the agreement was determined to be Rs.4 crores. As per the terms of the lease agreement, the lessee can cancel the lease by giving three months' notice in writing to the company. Turquoise Limited gave a notice on 1st October 2019 to vacate the property from 1st January, 2020. The fair value of such property was Rs. 58 crores as on 1st January, 2020.
On receiving such notice, Rainbow Limited has started the process of bifurcating the property into 10 identical units of equal size and sell it in the ordinary course of business. The company has incurred Rs.12 crores as the expenses towards such conversion upto 31st March, 2020. The bifurcation process is still in progress as at

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that date and the company estimates that they need to spend a further of Rs. 8 crores to complete the project, after which each of these units could fetch Rs. 10 crores.
Rainbow Ltd. has a wholly owned subsidiary Canyons Ltd. Rainbow Ltd. has approached Canyons Ltd for assistance and seeing the long term potential, the Subsidiary company has funded Rs. 20 lakhs to Rainbow Ltd. as interest-free loan. The loan shall either be repayable on demand or after a fixed term which will be mutually agreed upon by the parent and the subsidiary. The market rate of interest for similar loan is 12% p.a.

On 1st April, 2018, the company issued a convertible bond that matures in five years. The bond can be converted into ordinary shares at any time. Rainbow Limited has calculated that the liability and equity components of the bond areRs. 80 lakhs for the liability component and Rs.20 lakhs for the equity component, giving a total amount of the bond of Rs. 1 crore. The interest rate on the bond is 8% and local tax legislation allows a tax deduction for the interest paid in cash. The local tax rate is 30%.

In order to fund an upcoming project, Rainbow Limited borrowed Rs. 5 crores from a scheduled bank during 2019-20. The loan carries market interest rate and is repayable in 3 years. Given that the company invested a significant amount of time preparing the loan documentation and obtaining necessary approvals, Rainbow Limited has requested the bank to include an extension option. Accordingly, if the company so requires, it will have the option to extend the period of the loan at market rates prevailing at that date.

On 1st January, 2020, Rainbow Limited acquired a 60% stake in Shadow Limited. The cash consideration payable was Rs. 3 crore to be paid immediately, and Rs.1.21 crores after two years. The fair value of net assets of Shadow Limited at acquisition date wasRs. 5 crores. Rainbow Limited has calculated that its cost of capital is 10%. Non-controlling interest is measured at the proportionate share of identifiable net assets.

Rainbow Limited had purchased equipment P on 1st April, 2018 for Rs. 1 lakh and this had an estimated useful life of 10 years, with a residual value of zero. The asset is depreciated on a straight line basis. On 31st March, 2020, Rainbow Limited has revalued equipment P to
Rs. 1.04 lakhs.

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Questions

1.1 Calculate the deferred tax liability arising on the convertible bond as at the 2 year ending 31st March, 20.

(a) Rs. 30,00,000. (b) Rs. 2,40,000.

(c) Rs. 6,00,000. (d) Rs. 24,00,000.

1.2 Calculate the amount of goodwill/capital reserve arising upon acquisition of Shadow Limited.

(a) Rs. 1 crore .goodwill

(b) Rs. 80 lakhs of capital reserve.

(c) Rs. 20 lakhs goodwill.

(d) Rs. 41 lakhs of goodwill.

1.3 The three year term loan obtained from the bank contains an option to extend the period of the loan at market rates prevailing at that date. State which of the following is correct:

(a) It is not an embedded derivative.

(b) It is an embedded derivative closely related to the loan.

(c) It is an embedded derivative but not closely related to the loan, so it needs to be separately accounted for.

(d) It is an embedded derivative but not closely related to the loan, so no further accounting is required.

1.4 What is the annual depreciation charge on equipment P for years 3 to 10 and what is the amount of revaluation surplus that can be transferred to retained earnings annually?

(a) Annual depreciation charge will be Rs.10,000 and an annual transfer of Rs. 3,000 can be made from revaluation surplus to retained earnings.

(b) Annual depreciation charge, will be Rs.10,000, however, annual transfer from revaluation surplus to retained earnings is not permitted.

(c) Annual depreciation charge will be Rs.13,000 and an annual transfer of Rs. 3,000 may be made from revaluation surplus to retained earnings.

(d) Annual depreciation charge will be Rs. 13,000, however, annual transfer from revaluation surplus to retained earnings is not permitted.

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1.5 The CFO of Rainbow Limited is concerned that there may be an impairment of goodwill in one of the subsidiary companies. Clarify how impairment, if any, will be accounted for by the Parent company:

(a) It will always be deducted in full from the parent company retained earnings.

(b) It will be apportioned between the parent company and the Non-Controlling Interest (NCI) when the NCI is valued at fair value.

(c) It will never be apportioned between the parent company and the NCI

(d) It will be apportioned between the parent company and the NCI where the NCI is valued using the proportionate method.

(2 x 5 = 10 Marks)

1.6 Suggest the suitable accounting treatment, How will entity measure the right of use (ROU) asset and lease liability initially and at the end of 31/03/2020 including amount to be charged to profit & Loss account?

(6 Marks)

1.7 In regards to the property previously leased to Turquoise Limited, analyse the accounting implications of the bifurcation currently in progress under the relevant Ind AS and prepare a note on the classification, measurement and disclosure as at 31st March, 2019.

(4 Marks)

1.8 How should Rainbow Limited account for the interest-free loan Taken from Canyons Limited, under the following scenarios:

Scenario A: The loan is repayable on demand.

Scenario B: The loan is repayable after 5 years.

Provide necessary journal entries under both scenarios, in the books of Rainbow Limited and Canyons Limited for year 1.

(5 Marks)

Case Study 2

Makers Ltd. is engaged in the business of manufacturing a number of products including moulds, dies and machinery. They have a wide customer base in automobile, infrastructure, construction and other sectors both within India and abroad.

Entity Makers Ltd (lessee) entered into an agreement to take on lease a floor of building from Entity Y (lessor) for a period of 5 years. At commencement of lease, Entity Makers ltd pays INR 10,00,000 as interest-free refundable security deposit to Entity Y to protect its (Y's) interest in the property. Entity Makers Ltd's effective interest rate is 10%. Entity X expects to obtain economic benefits from the right of use evenly over the term of the lease and accordingly amortises the right of use on a straight-line basis.

Entity X (lessee) enters into an arrangement with Entity Makers Ltd to lease 10,000 square feet of office space for a period of 10 years. The annual lease payments are INR 100,000 in the first year, increasing by 5 percent each year thereafter, payable in arrears. The economic life of office space is 40 years. The lease term is not for a major part of the remaining economic life of the office space (40 years), and the present value of the lease payments is not substantially all of the fair value of the office space. Furthermore, the title does not transfer to Entity X as a consequence of the lease and the lease does not contain an option for Entity X to purchase the office space. Besides, the asset is not specialised such that it clearly has an alternative use to Entity Makers Ltd. at the end of the lease term. Thus, on a holistic evaluation of the terms of the lease, Entity Makers Ltd determines that it does not transfer substantially all the risks and rewards incidental to ownership of an underlying asset. Accordingly, the lease is classified by Makers Ltd as an operating lease.

At the beginning of Year 6, (2019-20) Entity X and Makers Ltd agree to amend the original lease for the remaining 5 years to include an additional 10,000 square feet of office space in the same building for an annual fixed payment of INR 150,000. The modified lease continues to be classified as an operating lease.

Makers Ltd. acquired 65% of shares on 1st June, 2019 in D Limited which is engaged in production of components of machinery. D Limited has 1,00,000 equity shares of Rs. 10 each. The quoted market price of shares of D Limited was Rs.12 on the date of acquisition. The fair value of D Limited's identifiable net assets as on 1st June, 2019 was Rs. 1,05,20,000.

Makers Limited wired Rs.75,00,000 in cash and issued 50,000 equity shares as purchase consideration on the date of acquisition. The quoted market price of Makers Limited on the date of issue is Rs. 25 per share.

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Makers Limited also agrees to pay additional consideration of Rs. 15,00,000, if the cumulative profit earned by D Limited exceeds Rs. 1 crore over the next three years. On the date of acquisition, D Limited assessed and determined that it is considered probable that the extra consideration will be paid. The fair value of this consideration on the date of acquisition is Rs. 10,00,000. D Limited incurred Rs. 1,50,000 in relation to the acquisition. It measures Non- controlling interest at fair value.

Additional information:
Makers Ltd. has identified five segments (denoted as A to E below, for ease of reference)

Segment	Sales		Total Sales	Profit	Assets
	Exports	Domestic			
A	1,20,00,000	-	1,20,00,000	10,00,000	2,00,00,000
B	2,50,00,000	80,00,000	3,30,00,000	30,00,000	15,50,00,000
C	4,50,00,000	-	4,50,00,000	61,00,000	18,00,00,000
D	2,70,00,000	60,00,000	3,30,00,000	30,00,000	20,00,00,000
E	40,00,000	50,00,000	90,00,000	9,00,000	1,50,00,000
		TOTAL	**13,20,00,000**	**1,40,00,000**	**57,00,00,000**

Makers Ltd. has entered into an lease for new office space for a period of 10 years from October 1, 2019. The escalation clause of the lease agreement states that the lease rent shall be escalated by 12% after completion of every 3 years. The general inflation rate in the economy is 5%. The initial lease rent agreed per month is Rs.85,000.

The company has an identifiable asset QR with a carrying amount of Rs. 10,00,000. Its recoverable amount is Rs. 6,50,000. The tax base of QR is Rs. 8,00,000 and the tax rate is 30%. Impairment losses are not tax deductible. Makers Ltd. expects to continue to earn profits in future.

Makers Ltd. acquired the trademark for a product from ABC Ltd. in 2008-09 for Rs. 8,00,000. The trademark is expected to have an indefinite useful life. The carrying amount as on 1st April, 2019 is Rs. 8,00,000. Now due to competition, the sales of the product have declined by 25%. The management has made assessment and has ascertained that the trademark will continue to have indefinite useful life. The recoverable amount is ascertained as Rs. 6,00,000.

Questions

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2.1 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.

2.2 What is the amount to be charged to the statement of profit and loss towards lease rent for the new office space for the year ended March 31, 2020?

(a) Nil

(b) Rs. 9,97,989.

(c) Rs. 5,87,935.

(d) Rs. 11,75,869.

2.3 For the identifiable asset QR, what would be the impact on the deferred tax asset/ liability at the end of the period?

(a) Nil impact.

(b) Deferred tax asset will have a closing balance of Rs.1,05,000.

(c) Deferred Tax asset will have a balance of Rs.60,000.

(d) Deferred tax asset will have a balance of Rs.45,000.

2.4 In respect of the trademark with indefinite life, Makers Ltd. seeks your advice on the appropriate treatment from following:

(a) The entity can continue with the same carrying amount of Rs.8,00,000.

(b) The entity can adopt amortisation for the amount of Rs.6,00,000.

(c) The entity has to test the asset for impairment, as an external unfavourable event had occurred and reduce the carrying amount to Rs.6,00,000.

(d) The entity is required to test the trademark for impairment every year and accordingly, the carrying amount will be reduced to Rs.6,00,000.

2.5 Makers Ltd. is evaluating a proposal to acquire the shares of C Ltd., a competitor. The company will proceed only if they will have a controlling stake, in accordance with the applicable accounting standards. Help them identify which one of the following situations will fail their objective, i.e., they are unlikely to have control over C Ltd.?

(a) Acquiring 56% of total shares of C Ltd and being able to elect 3 out of 5 directors on its Board.

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(b) Acquiring 65% of total shares with decisions requiring unanimous consent of all shareholders.

(c) Owning 40% of the total shares and having the majority of voting rights in C Ltd.

(d) Having currently exercisable options which would effectively result in 60% ownership of total shareholding.

(2 x 5 = 10 Marks)

2.6 How should Entity Makers ltd account for interest-free deposit paid to Entity Y?

(5 Marks)

2.7 How would Entity Makers Ltd account for the modification in the lease contract? (Assuming IND AS 116 is Followed/ Applied From the Beginning of Lease.)

(6 Marks)

2.8 How will the acquisition of D Ltd. be accounted by Makers Limited, under Ind AS 103? Prepare detailed workings and pass the necessary journal entries. Aslo state the various options for accounting Gain on Bargain purchase ?

(4 Marks)

Case Study 3

Your advisory client Gamma Limited is engaged in manufacturing and retail activities. Gamma Ltd entered into the following transactions during the year ended 31st March 2020.

(1) Entered into a speculative interest rate option costing Rs. 10,000 on 1st January 2020 to borrow Rs. 60,00,000 from ICICI Bank commencing 31st March 2012 for 6 months at 4%. The value of the option at 31st March 2020 was Rs. 15,250.

(2) Purchased 6% debentures in Y Ltd. on 1st April 2019 (their issue date) for Rs. 1,50,000 as an investment. Z Ltd. intends to hold the debentures until their redemption at a premium in 5 years' time. The effective rate of interest of the bond is 8.0%

(3) Purchased 50,000 shares in X Ltd. on 1st July 2019 fort Rs.3.50 each as investment. The share price on 31st March 2020 was Rs. 3.75.

While preparing the financial statements for the year ended 31st March, 2020, Gamma Limited has observed two issues in the previous year Ind AS financial statements (i.e. 31st March, 2019) which are as follows:

Issue 1:

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The company had presented certain material liabilities as non-current in its financial statements for periods as on 31st March, 2019. While preparing annual financial statements for the year ended 31st March, 2020, management discovers that these liabilities should have been classified as current. The management intends to restate the comparative amounts for the prior period presented (i.e., as at 31st March, 2019).

Issue 2:
The company had charged off certain expenses as finance costs in the year ended 31st March, 2019. While preparing annual financial statements for the year ended 31st March, 2020, it was discovered that these expenses should have been classified as other expenses instead of finance costs. The error occurred because the management inadvertently misinterpreted certain facts. The entity intends to restate the comparative amounts for the prior period presented in which the error occurred (i.e., year ended 31st March, 2019).

Additional information:
Gamma Ltd. granted share options to one of its technical directors on the condition that he will not work with a competitor (i.e., non-compete clause) for a period of three years. The fair value of the award at the date of the grant is Rs. 2,00,000, including the effect of the non-compete clause.
Gamma Ltd. has inventory of raw material Y of 10,000 units as at 31st March, 2020 with a carrying amount of Rs.100 each. The current market value of that raw material is Rs.95 each. Gamma Ltd. intends to use the raw material to manufacture a component to be used by a customer. Gamma Ltd. estimates costs to completion and sale of Rs.50 each and a selling price for the component is estimated to beRs. 145 each.

Gamma Limited sold a machinery Z for Rs.9,00,000, to a new customer. To get into long term relationship with the customer, the terms of sale also include after sales service to be provided for next three years free of cost. The company also sells the sales service contract separately where the customer buys it after the initial warranty period at Rs.1,00,000.

The company has stores across India. It deals mainly with three products A. B, and C. The company has a policy of refunding the entire purchase money provided the buyer returns the product without any damage within a period of 15 days in respect of Product A and B, and 6 months in respect of Product C. This policy has not been mentioned in any their written documents nor has been communicated in any other media. However, it is widely known. The company has duly complied with this policy in the past. The accountant has made an estimate, based upon past experience and the

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average probability that the cost involved in relation to the product return policy for each of the product is as follows:

	Rs.
Product A	1,50,000
Product B	2,50,000
Product C	5,00,000
Total	**9,00,000**

The management is of the view that no provision for returns needs to be created as there is no legal obligation on the part of the company.

Gamma Ltd. Subsidiary X ltd which has 500 million equity shares as on 31.3.2019 as well as on 31.3.2020. lts net profit for the years 2018-19 & 2019-20 were Rs.600 million and 800 million respectively.

Effective tax rate of the entity is 23%.

X Ltd has issued 10 million 12% Convertible Debentures of Rs.100 each on 1.1.2019, which are optionally convertible into 10 equity shares on 31.12.2025.

Questions

3.1 What is the value of raw material Y of Gamma Ltd. as per applicable Ind AS?

(a) Rs.9,50,000. (b) Rs.11,00,000.
(c) Rs.10,00,000. (d) Rs.16,00,000.

3.2 How should the revenue be recognised in the books of account for the sale of machinery Z?

(a) Rs.9,00,000 is to be recognised as revenue in the year of sale.
(b) Rs.9,00,000 is to be recognised at the end of three years after sale.
(c) Rs.9,00,000 is to be recognised in the year of sale and Rs.1,00,000 to be spread over next three years.
(d) Rs.8,10,000 is to be recognised in the year of sale and Rs. 90,000 to be spread over next three years.

3.3 Your advice is sought on the correct approach for Gamma Ltd.'s policy on return of Products A, B and C.(Ignoring IND AS 115)

(a) The provision has to be created as conservative policy has to be followed in accounting.
(b) The provision need not be created as the company is not under any legal obligation to return the purchase money.

(c) Provision has to be created for Rs. 9,00,000 as there exists a possibility of a future Obligation.

(d) The entity has to create a liability for Rs.9,00,000 (or such amount as may be determined after adjustment of the time duration remaining) as there exists a present obligation as a result of past event.

3.4 What is the correct accounting treatment under Ind AS for the share options granted to Gamma Ltd.'s technical director?

(a) Gamma Ltd. should recognise an expense of Rs. 2,00,000 over the period of three years and cannot reverse the expense recognised even if the director goes to work for a competitor and loses the share options.

(b) Gamma Ltd. should recognise an expense of Rs.2,00,000 over the period of three years and can reverse the expense recognised in case the director goes to work for a competitor and loses the share options.

(c) Gamma Ltd, should recognise an expense of Rs. 2,00,000 immediately and cannot reverse the expense recognised even if the director goes to work for competitor and loses the share options.

(d) Gamma Ltd. should recognise an expense of Rs. 2,00,000 immediately and can reverse the expense recognised in case the director goes to work for a competitor and loses the share options.

3.5 The CFO of Gamma Ltd. is trying her best to understand the high level differences between IFRS and US GAAP. Which of the following is the correct hierarchy under US GAAP hierarchy for determining the selling price of a deliverable?

(a) First, the Vendor-Specific Objective Evidence must be used, if available. If not, then Third Party Evidence is used. If neither prices are available, then the entity must make its Best Estimate of Selling Price.

(b) First, the Best Estimate of Selling Price must be used, if available. If not, then Vendor- Specific Objective Evidence is used. If neither prices are available, then the entity must obtain Third Party Evidence.

(c) First, Third Party Evidence must be used, if available. If not, then Vendor-Specific Objective Evidence is used. If neither prices are available, then the entity must make its Best Estimate of Selling Price.

(d) First, Third Party Evidence must be used, if available. If not, then Vendor-Specific Objective Evidence is used. If neither prices are available, then the entity must use Cost plus a Reasonable Margin.

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(2 x 5 = 10 Marks)

3.6 Compute Basic and Diluted EPS of X Ltd on 31.3.2019 and 31.3.2020 (Ignore need to Bifurcate convertible debentures into Debt & Equity)

(4 Marks)

3.7 You are required to show the accounting treatment of Financial Instruments and relevant extracts from the financial statements for the year ended 31st March 2020. Gamma Ltd. only designates financial assets as at fair value through profit or loss where it is unavoidable.

(7 Marks)

3.8 What is your analysis and recommendation in respect of the issues noted with the previously presented set of financial statements for the year ended 31st March, 2020?

(4 Marks)

Case Study 4

Kapsch Telecom Inc. is an American corporation that outsources some of its product engineering work to SasTech Ltd. in India. Both the parties have a long-term business relationship with each other – probably since more than 15 years.

In those 15 years, there have been multiple changes in management of both the parties. Kapsch has undergone many changes in the ownership and leadership in the last decade or so. In the outsourcing industry, it's a customary practice to request the customers for rate increase due to inflation and o ther factors that are specific to the contract.

Off-late there have been many instances of dissatisfaction from the customer due to attrition rate. Attrition refers to number of people leaving a company or a team. Attrition in the team is one of the biggest problems for Kapsch due to process-related hassles like interview of the replacement candidates, access to the file-sharing system and a few other factors.

SasTech Ltd. has been pressured for delivery and also forced to cut down the bill rate thereby reducing the profit margins. SasTech has an Offshore Development Centre (ODC) of 500 FTEs (Full-time employees) and an onsite support of Ten FTEs who work at the Kapsch location in USA.

ODC is a specific designated area within the company's premises. It requires special access to both employees and visitors who wish to enter into the ODC area. Even employees who are part of the same company but belong to team(s) other than the ODC can't enter the ODC area with their regular access card. Internet and other IT security is also special to the ODC through a dedicated leased-line which has a probability of 0.4% downtime.

Last contract with Kapsch, reviewed by both the parties, was almost 3 years ago. As a finance prime at SasTech Ltd., you have been asked by the Business Head to work closely with the Delivery Head and the legal team to look into the financial aspects of the contract.

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Multiple scenarios were worked out and many rounds of discussion happened but there was no satisfactory response from both the parties towards the closure of negotiation. Finally, after 4 months of continuous follow-up, con-calls and the intervention of SasTech's CEO, the following key terms were agreed and accepted by both the parties: (simplified extracts)

1. The monthly bill rate per FTE shall stand revised to USD 4400 from USD 4200 earlier for standard billing hours of 1920 per annum per ODC FTE.
2. Bill rate for Onsite FTEs shall stand revised to USD 11,000 per month from USD 10,500 earlier.
3. SasTech shall provide a buffer headcount of 10% (earlier 7%) of the total FTEs working in the ODC.

   (Buffer headcount is usually kept as replacement for any absent FTEs or loss of working hours due to any reason. The Buffer headcount is also trained on the job for the eventuality of attrition in the project. Buffer headcount is not billed to the client but absorbed as direct contract cost.)
4. Other terms and conditions of the contract shall remain the same except that the following new terms will be inserted through Annexure which shall form an integral part of the contract:

a. Performance Bonus will be payable to SasTech at the rate of 10% of the quarterly billing done if the average billed hours of the ODC exceed 520 hours per FTE per quarter and the attrition rate is below 5% during that quarter.

b. Attrition Penalty will be payable by SasTech as per the following table:

Attrition Rate during the quarter in the ODC	Attrition Penalty as a percentage of Quarterly billing done
6% to 8%	3.5%
8% to 10%	4.5%
10% to 12%	6.0%
More than 12%	10.0%

5. The process of the timesheet approval shall remain the same except that the Project Manager of Kapsch in USA shall have a final approval authority. (Earlier, ODC manager in SasTech used to aggregate and ratify the timesheet and get the same approved by the Onsite lead of SasTech in USA and the same was counter-approved by the Project Manager from Kapsch. Now the project manager is changed since last 2 years.)
6. Billing will continue to be done on a quarterly basis and the credit period shall remain as 45 days from the end of last calendar day of the quarter for which billing is done.
7. SasTech shall continue to invoice at standard bill hours on a quarterly basis even when the actual billable hours as per final timesheet are more or less than the standard hours per FTE per month unless the actual billable hours fall below 150 per month per FTE. In that case the billing shall be done on actual billable hours. Actual billable hours are also used for billing in the quarter when SasTech is eligible for performance bonus.
8. Performance Bonus, if any, shall be billed separately within 20 working days from the end of the quarter in which such bonus becomes payable as per the contract.
9. Penalty, if any, shall be deducted from the latest quarterly bill received by Kapsch after the end of the relevant quarter.
10. Both the parties to the contract shall endeavour to close the approval process of billable hours within 7 working days from the end of each quarter.
11. Work done by Buffer FTEs, if any, shall not be counted for billing.

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Following is the timesheet and attrition data for four quarters since the renewed contract has come into force.

Period	Hours approved by SasTech	Hours approved by Kapsch	Attrition rate
Quarter 1 Financial Year 2019-2020	2,41,500	2,41,415	6.0%
Quarter 2 Financial Year 2019-2020	2,62,500	2,62,319	4.5%
Quarter 3 Financial Year 2019-2020	2,39,000	2,38,585	9.2%
Quarter 4 Financial Year 2019-2020	2,23,500	2,23,500	7.0%

Revenue from Kapsch accounts for more than 20% of the total revenue of SasTech Ltd. every year. However, Kapsch was not shown as a separate reportable segment until last audited annual financials of the company.

Since SasTech is a listed company on Bombay Stock Exchange as well as National Stock Exchange, the company has to publish quarterly financial information after the limited review of the auditors. The carrying amount of SasTech's ODC asset (for Kapsch) is Rs. 129 Lacs (after considering impact of contract with Kapsch during the year) as on 31st March 2020.

As a finance prime your help is required by the head of R2R (Record to report) team during each of the quarter close before the financial information is submitted to the auditors for limited review.

Questions

4.1 The Head of R2R was not aware of this latest contract with Kapsch in so much of details. You have discussed with him the main points of the contract including the Performance Bonus and Attrition Penalty. The Consideration agreed by both the parties in this contract is __________

(a) Variable and requires allocation to distinct performance obligation

(b) Variable but does not require specific allocation to distinct performance obligation

(c) Composite consideration

(d) Composite consideration with distinct performance obligations

4.2 SasTech Ltd. has decided to make provision for attrition penalty at the beginning of each quarter instead of booking that amount as loss in the case of liability of pay penalty. Historically, Kapsch ODC has seen at attrition rate of 7%. If the same attrition percentage is used for provision of attrition penalty what will be the provision amount for Q1FY19-20? Assume standard billing hours of 1920 per annum per FTE in ODC.

(a) USD 2,30,000

(b) USD 2,31,000

(c) USD 2,32,000

(d) USD 2,33,000

4.3 "Now that the contract has changed substantially and Kapsch accounts for about 20% of company's revenue we may have to show this as a separate operating segment", said the Head of R2R at SasTech Ltd. In view of the principles of IFRS, what is your view?

(a) Since there is only one such contract, separate reportable segment treatment is not called

for.

(b) Head of the R2R team is right. It needs to be reported as a separate segment.

(c) Just a disclosure as special contract is required.

(d) Provision for Attrition Penalty is required.

4.4 The company is likely to get performance bonus for Quarter 2 Financial year 2019-2020. The final approval of timesheet has been received from Kapsch on 6th working day from the end of the quarter. Compute the amount of performance bonus that can be recognized as revenue before the financial information is passed on to the auditors for limited review.

(a) USD 0.72 million

(b) USD 0.71 million

(c) USD 0.73 million

(d) USD 0.74 million

4.5 What are the two factors that compelled the organisation to treat Kapsch contract as a separate reportable segment?

(a) Final approval process for timesheet and attrition

(b) Performance bonus and attrition penalty

(c) Threshold for segment recognition and total contract revenue

(d) Standard hours mentioned in the contract.

(2 x 5 = 10 Marks)

4.6 If SasTech Ltd. has reported this contract as a separate reportable segment "Revenue from special contracts", prepare "Notes to account" to disclose the amount of adjustments made on account of performance bonus and attrition penalty for Financial Year 2019-2020. Working notes should be part of your answer but not the part of disclosure.
For calculation purposes assume 1 USD = Rs. 65.

(6 Marks)

4.7 If final approval for timesheet for Q2FY19-20 was not received as on the date of preparing financials but received subsequently due to delay from Kapsch (as the concerned person was travelling), should the company recognise the performance bonus as Unbilled Revenue (classified as current asset in the balance sheet) or treat it as a revenue? Justify your answer citing specific reference from relevant IFRS and facts of the case.

(4 Marks)

4.8 As on 31st March 2020, the ODC has no other liability except the provision for attrition penalty for Quarter 4 Financial Year 2019-2020. Disclose the amount of Segment revenue, Segment assets and Segment liabilities under "Revenue from Special Contracts" if there are no other contracts of similar nature for SasTech Ltd. For calculation purposes assume 1 USD = Rs. 65.

(5 Marks)

Case Study 5

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Main Bank Ltd. holds certain loans of Rs. 10,000 that yield 18% interest per annum for their estimated lives of 9 years. The fair value of these loans, after considering the interest yield is estimated at Rs. 11,000. Main Bank securitizes the principal component of the loan plus the right to receive the interest at 14% to Beta Ltd., a special purpose entity, for Rs. 10,000.

Out of the balance interest of 4% it is stipulated that half of such balance interest namely, 2% will be due to Main Bank Ltd. as a fee for continuing to service the loans. The fair value of the servicing asset so created is estimated at Rs. 350. The remaining half of the interest is due to Main Bank Ltd. as an interest strip receivable, the fair value of which is estimated at Rs. 650.

During 2018-2019, Main Bank Ltd.'s subsidiary Sub Bank Ltd. originates 2,000 bullet loans with a gross carrying amount of Rs. 50 Lakhs. It has decided that the portfolio would be segregated between Individual Housing Loans and Non-Individual Housing Loans, on the basis of shared credit risk characteristics at initial recognition. Individual housing loans portfolio comprises 1,000 loans with a gross carrying amount of Rs. 2,000 per client on average, and a total gross carrying amount of Rs. 20 Lakhs. The Non-Individual housing loans comprise 1,000 loans with a gross carrying amount of Rs. 3,000 per client. The historical default rate for next 12 months is 4 borrowers in Individual Housing Loan and 2 borrowers in Non-Individual Housing Loans. Assume that there are no transaction costs or fees, and that the loan contracts do not include any option for prepayment or call. Consider that the EIR is 10%.

Main Bank has a number of corporate clients who regularly enter into derivatives (mainly forward contracts and options) to manage the volatility on their forecast cash inflows/outflows arising from sales and purchases. There are also some large companies that enter into External Commercial Borrowings (ECB loans) which are typically structured as a variable rate loan with a floating-to-fixed interest rate swap. Main Bank is frequently posed with questions by these clients on whether they should adopt hedge accounting. They also periodically request valuation statements that are inclusive of Credit Valuation Adjustment and Debit Valuation Adjustment (CVA and DVA) for derivatives.

Additional information:

Main Bank has a debt factoring arrangement for its customer A. Main Bank agreed to pay Rs.91.5 lakhs, less a servicing charge of Rs.1.5 lakhs (net proceeds Rs.90 lakhs), in exchange for 100% of the cash flows from short term receivables of customer A. According to customer A, the receivables have a face value of Rs. 100 lakhs and carrying amount of Rs. 95 lakhs. The customers will be instructed to pay the amounts to Main Bank. Customer A also writes a guarantee to Main Bank that it will reimburse any credit losses upto Rs. 5 lakhs, over and above the expected credit losses of Rs. 5 lakhs and losses of up to Rs. 15 lakhs are considered reasonable. The guarantee is estimated to have a fair value of Rs. 0.5 lakhs.

Questions

5.1 The middle office of Main Bank Ltd. is examining the financial statements of its customers (i.e., borrowers) in order to ensure that loan covenants are being met, especially with respect to debt-equity ratios. Assist them in determining which of the instruments will qualify as equity in their entirety under Ind AS:

(a) Redeemable debentures with discretionary dividend.

(b) Optionally convertible redeemable preference shares.

(c) Debentures convertible into a fixed number of instruments, at the option of the issuer.

(d) Debentures convertible into a fixed number of instruments, at the option of the holder.

5.2 Some of Main Bank's customers are in troubled times and they are going through Strategic Debt Restructuring i.e. renegotiating with Main Bank the terms of their debt. Help them understand the requirements of Ind AS 109 so they can assess the accounting implications for the loan in their books:

(a) A qualitative assessment is sufficient, as the counterparty for the modified loan is the same as before.

(b) Although the counterparty is the same since the two loans are considered as separate financial instruments, the old loan must be mandatorily derecognised and the renegotiated loan has to be recognised.

(c) A qualitative assessment may not be sufficient and a quantitative assessment may be required. If there is substantial modification, the old loan need not be derecognised.

(d) A qualitative and quantitative assessment may be needed. If there is substantial modification, the old loan must be derecognized and the renegotiated loan has to be recognised.

5.3 Disclosures of fair value are not required when:

(a) Fair value cannot be estimated.

(b) Fair value assumptions are described in accounting policies.

(c) The carrying amount is a reasonable approximation of fair value.

(d) Three level fair value hierarchy is provided in the notes to accounts.

5.4 Which of the following instruments is not an example of a derivative contract?

(a) Total return swap.

(b) LIBOR linked debentures.

(c) Credit Default Swap.

(d) Written treasury bond option.

5.5 In respect of Main Bank's debt factoring arrangement for its customer A, which of the following statements is correct?

(a) Continuing involvement asset must be recognised along with the associated liability.

(b) Continuing involvement asset must be recognised but there is no associated liability.

(c) There is continuing involvement asset but the associated liability must be recognized.

(d) There is no continuing involvement in the receivables of customer A.

(2 x 5 = 10 Marks)

5.6 You are required to assist Main Bank in analyzing the securitisation transaction. Compute the fair value of the securitised component of the loan and the amortisation of the carrying amount based on related fair values.

Pass journal entries in the books of Main Bank upon securitisation of these loans.

(6 Marks)

5.7 Calculate the loss rate approach in the books of Sub-Bank for both Individual Housing Loans and Non-Individual Housing Loans. **(4 Marks)**

5.8 Explain why hedge accounting may be helpful to Main Bank's corporate clients. Briefly

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outline the need and requirements of CVA and DVA for derivative contracts.

(5 Marks)

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