J.K. SHAH®

TEST SERIES

Evaluate Learn Succeed

SUGGESTEDANSWERS

CA FINAL

Test Code – JK-FR-22

Date – 23-09-2020

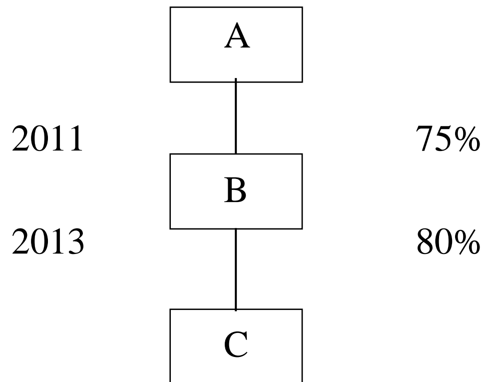
Head Office: Shraddha, 3rd Floor, Near Chinai College, Andheri E, Mumbai – 69

Tel: (022) 26836666

Answers

Q.1

(a)



Effective stake in C:

A Group (75% x 80%) = 60%

NCI = 40%

Working Notes:

1. Goodwill:

	A in B		B in C	
Consideration transferred	₹	₹	₹	₹
		1,10,000	(75% x 6,200)	4,650
Non-controlling interests	(25% × 140,000)	35,000	(40% x 7,500)	3,000
Fair value of identifiable Net Assets acquired:				
Share capital	100,000		10,000	
Retained earnings:	40,000		(2,500)	
		(140,000)		(7,500)
		5,000		150

5,150 **(6 Marks)**

J.K.SHAH CLASSES

2. Retained earnings:

	A ₹	B ₹	C ₹
Given	3,79,600	1,29,200	(1,000)
Pre-acquisition profit/losses		(40,000)	2,500
Post-acquisition profits		**89,200**	**1,500**
Group share			
In B Co. (89,200 x 75%)	66,900		
In C Co. (1,500 x 60%)	900		
Unrealized profit in inventories (4,000 x 1/2)	(2,000)		
Group retained earnings	**4,45,400**		

(2 Marks)

3. Non – controlling interest

	B ₹	C ₹
NCI at acquisition (working Note -1)	35,000	3,000
NCI in post-acquisition retained earnings [89,200 (WN- 2) × 25%] / [1,500 [WN- 2] ×40%]	22,300	600
Less: NCI share of investment in C Co. (6,200 × 25%)	(1,550)	-
	55,750	**3,600**

59,350

(4 Marks)

J.K.SHAH CLASSES

CONSOLIDATED BALANCE SHEET AS ON 31st MARCH 2020

	₹	₹
Assets		
Non-current Assets		
Freehold property		2,00,000
Plant and machinery		2,93,000
		4,93,000
Goodwill (Working note – 1)		5,150
		4,98,150
Current Assets		
Inventories (205,500 – 2,000)	2,03,500	
Financial Assets		
Receivables	2,17,000	
Cash at Bank	80,500	
		5,01,000
		9,99,150
Equity and Liabilities		
Equity Share capital		2,00,000
Retained earnings (Working Note – 2)		4,45,400
Shareholder funds		6,45,400
Non-controlling interests (Working Note -3)		59,350
Liabilities		7,04,750
Current liabilities		
Trade payables	2,27,400	
Tax	67,000	
		2,94,400
		9,99,150

(4 Marks)

(b)

Ind AS 116 states the following:-

An asset is typically identified by being explicitly specified in a contract. However, an asset can also be identified by being implicitlyspecified at the time that the asset is made available for use by the customer.”

In the given case, trucks are not identified explicitly or implicitly and hence the arrangement does not contain a lease.

(4 Marks)

J.K.SHAH CLASSES

Q.2

(a)

Computation showing segregation of liability and equity component

	Amt. (₹)
Present value (PV) of Principal ₹ 10 lakhs at the end of 3 years discounted at 12%: PV (Z.10 lakhs X 0.712)	7,12,000
PV of interest of ₹ 1 lakh annually in arrears for 3 years (₹ 1 lakh x 2.402)	2,40,200
Liability Component	9,52,200
Equity Component (Value of conversion option)	47,800
Proceeds from issue of convertible debentures (10,000 x100)	**10,00,000**

(2 Marks)

Debt is accounted for as per Ind As – 109 applying amortized cost method.

Date	Cash flows	Finance cost	Amortized cost adjustment	Amortized cost
1- Apr - 15	-9,52,200			9,52,200
31- Mar - 16	1,00,000	1,14,264*	14,264	9,66,464
31- Mar - 17	1,00,000	1,15,976**	15,976	9,82,440
31- Mar - 18	11,00,000	1,17,560***	17,560	10,00,000
IRR =	12%			

(2 Marks)

₹ 9,52,200 × 12% = ₹ 1.14,264

**₹ 9,66,464 × 12% = ₹ 1,15,976

***₹ 9,82,440 × 12% = 1,17,893 rounded off to ₹ 1,17,560 being balancing figure to make the amortized cost at ₹ 10 lakhs.

Internal rate of return (IRR) is the effective interest rate for the purpose of computing amortized cost.

J.K.SHAH CLASSES

Accounting entries:

Date	Particulars	Dr. (₹)	Cr. (₹)
1- Apr -15	Bank Account Dr. To Convertible Debentures (Liability Component) To Conversion Option (Equity Component)	10,00,000	 9,52,200 47,800
31- Mar -16	Finance Cost Dr. To Bank Account To Convertible Debentures (Liability Component)	1,14,264	 1,00,000 14,264
31- Mar - 17	Finance Cost Dr. To Bank Account To Convertible Debentures (Liability Component)	1,15,976	 1,00,000 15,976
31- Mar - 18	Finance Cost Dr. To Bank Account To Convertible Debentures (Liability Component)	1,17,560	 1,00,000 17,560
31- Mar - 18	Convertible Debentures (Liability Component) Dr. To Equity Share Capital Account To Share Premium Account (Issue of 2000 equity shares of ₹ 10 each at ₹490 premium. Market price of equity shares on the date of conversion is not relevant)	10,00,000	 20,000 9,80,000
31- Mar - 18	Conversion Option (Equity Component) Dr. To Share Premium Account (Conversion option value is transferred to share premium because on issue of shares this becomes part of share premium.)	47,800	 47,800

(4 Marks)

Note:

On conversion of a convertible instrument at maturity, the entity derecognizes the liability portion and recognizes it as equity. The original equity portion remains as equity (although it may be transferred from line item within equity to another).

There is no gain or loss on conversion at maturity.

(b)

Ind AS 115 provides that, "the objective when allocating the transaction price is for an entity to allocate the transaction price to each performance obligation (or distinct good or service) in an amount that depictsthe amount of consideration to which the entity expects to be entitled in exchange for transferring the promised goods or services to the customer".

In this case, there are two separately identifiable performance obligationsone being a sale of a photocopier machine and second being maintenancecontract for five years.

As per the Standard, to allocate the transaction price toeach performance obligation on a relative stand-alone selling price basis, anentity shall determine the stand-alone selling price at contract inception ofthe distinct good or service underlying each performance obligation in thecontract and allocate the transaction price in proportion to those stand-aloneselling prices.

For recognition of revenue, relative stand-alone selling price of the individualcomponents may be taken and the consideration allocated in proportion ofrelative fair values, i.e. 80,000:30,000. Hence, the sale of photocopiermachine should be recognised at ₹72,727 (₹1,00,000 x 8/11) when allother conditions for sale of photocopier machine are fulfilled and the revenuefrom maintenance services of ₹27,273 (100,000 x 3/11) should be theservice revenue recognised over a period of five years as per its stage of completion.

(6 Marks)

(c)

Ind AS 38 requires expenditure on research (or on the research phase of aninternal project) to be recognised as an expense when it is incurred. Likewise, it requires expenditure on development (or on the developmentphase of an internal project) to be recognised as an expense when it isincurred except where an entity can demonstrate compliance with the criterialaid down in the standard for inclusion of the expenditure in the cost of aninternally generated intangible asset.

Ind AS 38 states as follows:

"Expenditure on an intangible item that was initially recognised as an expense shall not be recognised as part of the cost of an intangible asset at a later date."

Ind AS 38 applies to those items of expenditure on an intangible item that were correctly recognised initially as an expense inaccordance with the requirements of the standard. If an item is incorrectlyrecognised initially as an expense, the correction of the error in a later periodin accordance with Ind AS 8 by including the expenditure in the cost of anintangible asset is not inconsistent with, and therefore does not tantamountto non-compliance of Ind AS 38.

In the given case, in determining the treatment of the relevant expenditure,the management made a mistake in using reliable information that was already available when the financial statements for the year ended 31 March2018 were approved for issue. Had the management not made the mistake,the said expenditure would have been capitalised rather than being expensed. The expensing of the expenditure in the financial statements forthe year ended 31 March 2018 thus represents a prior period error. Ind AS 8requires correction of material prior period errors by retrospectively adjusting the comparative financial information. When an entity retrospectively restatesits comparative information under Ind AS 8, it corrects the error in such away as if the prior period error had never occurred.

Thus, in the given case, the relevant expenditure would be retrospectivelyincluded in the cost of the relevant intangible asset.

(6 Marks)

Q.3

(a)

Ind AS 115, inter alia, states that, "An entity shall accountfor a contract modification as a separate contract if both of the followingconditions are present:

a) the scope of the contract increases because of the addition ofpromised goods or services that are distinct and

b) the price of the contract increases by an amount of consideration thatreflects the entity's stand-alone selling prices of the additionalpromised goods or services and any appropriate adjustments to thatprice to reflect the circumstances of the particular contract.

For example, an entity may adjust the stand-alone selling price of anadditional good or service for a discount that the customer receives,because it is not necessary for the entity to incur the selling-relatedcosts that it would incur when selling a similar good or service to anew customer".

In accordance with the above, it may be noted that a contract modificationshould be accounted for prospectively if the additional promised goods orservices are distinct and the pricing for those goods or services reflects theirstand-alone selling price.

In the given case, even though the remaining services to be provided are distinct, the modification should not be accounted for as a separate contract because the price of the contract did not increase by an amount ofconsideration that reflects the standalone selling price of the additionalservices. The modification would be accounted for, from the date of the modification, as if the existing arrangement was terminated and a new

contract created (i.e. on a prospective basis) because the remaining services to be provided are distinct.

AB Ltd. should reallocate the remaining consideration to all of the remainingservices to be provided (i.e. the obligations remaining from the originalcontract and the new obligations). AB Ltd. will recognise a total of₹4,20,000 (₹1,20,000 + ₹3,00,000) over the remaining four-year service period (one year remaining under the original contract plus three additional years) or ₹1,05,000 per year.

(7 Marks)

(b)

Allocation of proceeds of the bond issue: **(3 Marks)**

- Liability component	₹ 18,48,122
- Equity component	₹ 1,51,878
	₹ 20,00,000

This represents the present value of the principal and interest discounted at 9% ₹ 2,000,000 payable at the end of three years; ₹1,20,000 payable annually in arrears for three years.

The liability and equity components would be determined in accordance with Ind AS-32 Financial Instruments: Presentation. These amounts are recognized as the initial carrying amounts of the liability and equity components. The amount assigned to the issuer conversion option equity element is an addition to equity and is not adjusted.

Basic EPS Year 1: **(1 Marks)**

₹ 1,000,000/1,200,000 = Re. 0.83 per ordinary share

Diluted EPS Year 1: **(3 Marks)**

It is presumed that the issuer will settle the contract by the issue of ordinary share. The dilutive effect is therefore calculated in accordance with Ind AS-33.

(₹ 1,000,000 + ₹ 166,331*) / (1,200,000 +500,000**) = ₹ 0.69 per ordinary share

*Profit is adjusted for the accretion of ₹ 166,331 (₹ 1,848,122 × 9%) of the liability because of the passage of time.

**5,00,000 ordinary shares = 250 ordinary shares × 2,000 convertible bonds.

J.K.SHAH CLASSES

(c)

As per Ind AS 34, Interim Financial Reporting, the quarterly net profit should be adjusted and restated as follows:

(i) Bad debts of ₹ 1,64,000 have been incurred during current quarter. Out of this, the company has deferred 75% i.e. ₹ 1,23,000 to the next 3 quarters. This treatment is not correct as the expenses incurred during an interim reporting period should be recognised in the same period unless conditions mentioned in Ind AS 34 are fulfilled. Accordingly, ₹ 1,23,000 should be deducted from the net profit of the current quarter₹ 15,00,000. **(1 mark)**

(ii) Deferment of sales promotion expenses of ₹ 4,50,000 is not correct. It should be charged in the quarter in which the expenses have been incurred. Hence, it should be charged in the first quarter only. **(1 mark)**

(iii) Deferment of additional depreciation of ₹ 2,62,500 (₹3,50,000 x 75 %) is not correct.
it should be charged in the first quarter only. **(1 Mark)**

(iv) Deferment of extra-ordinary loss of ₹ 68,000 (1,36,000 x 50%) is not correct.
it should be charged in the first quarter only. **(1 Mark)**
Thus considering the above, the correct net profits to be shown in Interim Financial Report of the third quarter shall be ₹ 15,00,000 - ₹ 1,23,000 - ₹ 4,50,000 - 2,62,500 - 68000 = ₹ 5,96,500. **(2 Mark)**

Q.4

(a)

Ind AS 115 *inter alia,* states that, "an entity shall excludefrom an input method the effects of any inputs that, in accordance with theobjective of measuring progress do not depict the entity'sperformance in transferring control of goods or services to the customer".

In accordance with the above, Company X assesses whether the costsincurred to procure the air conditioners are proportionate to the entity'sprogress in satisfying the performance obligation. The costs incurred toprocure the air conditioners (₹10,00,000) are significant relative to the totalcosts to completely satisfy the performance obligation (₹40,00,000). Also,Company X is not involved in manufacturing or designing the air conditioners.

Company X concludes that including the costs to procure the air conditionersin the measure of progress would overstate the extent of the entity'sperformance. Consequently, in accordance Ind AS115, the entity adjusts its measure of progress to exclude the costs to procure the air conditioners from the measure of costs incurred

and from thetransaction price. The entity recognises revenue for the transfer of the airconditioners at an amount equal to the costs to procure the air conditioners (i.e., at a zero margin).

Company X assesses that as at March 2018, the performance is 20 per centcomplete (i.e., ₹6,00,000/₹30,00,000).

Consequently, Company Xrecognises the following-

As at March 31, 2018	**Amount in ₹**
Revenue	18,00,000
Cost of goods sold	16,00,000
Profit	2,00,000

Revenue recognised is calculated as (20 per cent × ₹40,00,000) +₹10,00,000.

(₹40,00,000 = ₹50,00,000 transaction price – ₹10,00,000 costs of airconditioners.)

Cost of goods sold is ₹6,00,000 of costs incurred + ₹10,00,000 costs ofair conditioners.

(6 Marks)

(b)

The amount recognized as an expense in each year is as follows:

Year	Expense for the year	Cumulative expense	Calculation of cumulative expense
31 December 2015	90,000	90,000	54 x 1,000 x 5 x 1/3
31 December 2016	1,57,000	2,47,000	57 x 1,000 x [(5 x 2/3) + (2 x 1/2)]
31 December 2017	138,000	3,85,000	55 x 1,000 x (5 +2)

(6 Marks)

(c)

In the financial statements of X Ltd the carrying amount of the debenture is allocated on the issue as follows: **(2 Marks)**

	₹
Liability component	
Present value of 20 half- yearly interest payments of ₹ 50, Discounted at 11% [(50 × 11.95)based on PVIFA@ 5.5% for 20 years]	597
Present value of ₹ 1,000 which is due in 10 years,discounted at 11% Compounded half yearly (PVIF@ 5.5% at the end of 20th year i.e. 0.343× 1000]	343
	940
Equity component (Balancing figure)	60
Total proceeds	**1,000**

The repurchase price is allocated as follows:
This will be done on 1" April, 2014 i.e. after 5 years from the date of issue.

	Carrying Value		Fair Value
Liability component:	₹	₹	₹
Present value of 10 remaining half-yearly interest Payments of ₹ 50, discounted at 11% and 8%, respectively. (PVIFA @ 5.5% for 10 Years i.e. 7.538 x 50) and (PVIFA @ 4% for 10 Years i.e. 8.1 x 50) respectively	377	405	(28)
Present value of ₹1,000 which is due in 5 years, discounted at 11% and 8%, compounded half yearly, respectively (PVIFA @ 5.5% for 10th Years i.e. 0.585 x 1,000) and (PVIF @ 4% at the end of 10th Year (i.e. 0.676 x 1,000) respectively	585	676	(91)
	962	1081	(119)
Equity Component	(60 same)	619 (b/f)	(559)
Total	**1,022**	**1,700**	**(678)**

(4 Marks)

X Ltd. recognises the repurchase of the debenture as follows:		
Liability component	Dr.	₹ 962
P&L	Dr.	₹ 119
To cash		₹ 1,081
(To recognises the repurchase of the liability compassed)		
Equity component	Dr.	₹ 60
Equity (Reserve & Surplus)	Dr.	₹ 559
To cash		₹ 619
(To recognises the cash paid for the Equity component)		

(2 Marks)

Q.5

(a)

Value of closing stock = ₹ 28,000 (2000 X 14)

Raw Material = ₹ 5

Direct Labour = ₹ 2

Direct Expenses = ₹ 3

Fixed Prodn OH = 4 (20000/5000)

13

(4 Marks)

(b)

	Carrying value	Tax base	Temporary difference
Non- current assets			
Assets subject to investment relief	63,000	28,000	35,000
Land	2,00,000	1,50,000	50,000
Plant and Equipment	1,00,000	90,000	10,000
Receivables			
Trade Receivables	73,000	80,000	(7,000)
Interest Receivables	1,000	-	1,000
Payables			
Fine	(10,000)	(10,000)	-
Interest payables	(3,300)	-	(3,300)
			85,700

(8 Marks)

	Temporary difference	Deferred tax @ 30%
Deferred tax liabilities	96,000	28,800
Deferred tax assets	(10,300)	(3,090)
		25,710

(2 Marks)

	Deferred tax @ 30 %
Deferred tax as at 1st January 2017	3,600
To other comprehensive income (30% × 50,000)	15,000
Profit or loss (balancing figure)	7,110
Deferred tax as at 31st December 2017	**25,710** **(2 Marks)**

J.K.SHAH CLASSES

(c)

The company purchased 100 sheep at an auction for ₹ 60,000 the transportation cost was ₹ 1,500 and the auctioneer's fees were ₹ 600 (1% of ₹ 60,000).

The fair value of the sheep on 31st December would be 59,400 (₹ 60,000 - 600) and it will be shown in the Balance Sheet. The transportation costs will not be considered as they are not considered a cost to sell according to Ind AS-41.

A loss of ₹ 2100 (1500+600) would be shown in the statement of profit and loss.

(2 Marks)

When the fair value of the sheep rises to ₹ 70,000 on 30th June 2016:

The Sheep will be measured at 69,300 (70,000-700)

A gain of ₹ 9,900 (69,300-59,400) would be reflected in the Statement of profit and loss.

(2 Marks)

Q.6

(a)

Management should initially recognized provision for ₹1,099 crores, being the present value of 1,200 crores discounted at 4.5% for 2 years:

(₹in Crores)

Year	Discount factor at 4.5%	NPV	Cash flow	Borrowings cost
	09157	1099	-	
1	0.9569	1148	-	49
2	1.000	1200	1200	52

(2 Marks)

Year (Beginning):

Expense A/c	Dr.	1099	
To Provision			1099

Year 1 (Closing):

Interest A/c (Expense)	Dr.	49	
To Provision			49

Year 2 (Closing):

Interest A/c (Expense)	Dr.	52	
To Provision			52

It the end of year 2, the provision a/c will show credit balance of 1200 crores Interest will be written off in profit and loss. **(3 Marks)**

(b)

As per Ind AS 103, the standard does not apply to "the acquisition of an asset or a group of assets that does not constitute abusiness. In such cases the acquirer shall identify and recognise the individual identifiable assets acquired (including those assets that meet thedefinition of, and recognition criteria for, intangible assets in Ind AS 38,*Intangible Assets*) and liabilities assumed. The cost of the group shall beallocated to the individual identifiable assets and liabilities on the basis oftheir relative fair values at the date of purchase. Such a transaction or eventdoes not give rise to goodwill".

In the given case, the acquisition of equipment and patent does not represent acquisition of a business.

The cost of the asset acquisition is determined based on the fair value of theassets given, unless the fair value of the assets received is more reliably determinable.

Thus, the entity should record the acquisition of the equipment and patent as INR 1,400 crores (the total fair value of the considerationtransferred).

Thus, the fair value of the consideration given, i.e., INR 1,400 crores isallocated to the individual assets acquired based on their relative estimatedfair values. The entity should records a gain of INR 300 crores for thedifference between the fair value and carrying value of the land.

The equipment is recorded at its relative fair value ((INR 500 / INR 1,500) ×INR1,400 = INR 467 crores).

The patent is recorded at its relative fair value ((INR 1,000 / INR 1,500) ×INR1,400 = INR 933 Crores).

(4 Marks)

(c)

The following shall be the accounting treatment

Particulars	**Amount**
Fair value of previous 10% interest held	1,60,000
Fair value of additional 25% (amount paid)	4,00,000
	5,60,000

Goodwill is calculated as follows:

Cost of investment in associate	5,60,000
Fair value of identifiable net assets acquired (800,000*35%)	2,80,000
Goodwill	2,80,000

(3 Marks)

Journal entry: (₹)

Particulars		**Dr. / Cr.**
Amount		
Investment A/c (Including goodwill of ₹ 280,000)	Dr.	560,000
OCI (Equity)	Dr.	60,000
To Cash	Cr.	400,000
To Investment (FVOCI)	Cr.	160,000
To Retained earnings (Equity)	Cr.	60,000

(3 Marks)

(d)

Computation of Goodwill / Capital reserve on consolidation as per Ind AS 103

Particulars	INR
Cost of investment:	
Share exchange (50,000 x 25)	12,50,000
Cash consideration	50,00,000
Contingent consideration	9,80,000
Consideration transferred at date of acquisition [A]	72,30,000
Fair value of non-controlling interest at date of acquisition (1,00,000 x 35% x 12) [B]	4,20,000
Total [C] = [A] + [B]	76,50,000
Net assets acquired at date of acquisition [D]	(80,00,000)
Gain on Bargain Purchase /Capital Reserve [D] – [C]	3,50,000

In a business combination, acquisition-related costs (including stamp duty) are expensed in the period in which such costs are incurred and are not included as part of the consideration transferred. Therefore, ₹ 1,50,000 incurred by D Ltd. in relation to acquisition, will be ignored by Makers Ltd. **(3 Marks)**

Journal entry at the date of acquisition by Makers Limited as per Ind AS

		₹	₹
Identifiable net assets	Dr.	80,00,000	
To Equity share capital (50,000 x 10)			5,00,000
To Securities Premium (50,000 x 15)			7,50,000
To Cash			50,00,000
To Provision for contingent consideration to D Ltd.			9,80,000
To Non-controlling Interest			4,20,000
To Capital Reserve			3,50,000

(2 Marks)

J.K.SHAH CLASSES