MOCK TEST PAPER

FINAL (NEW) COURSE: GROUP – II

PAPER 6E –GLOBAL FINANCIAL REPORTING STANDARDS

Candidates are required to answer any four case studies out of five case studies.

Wherever necessary, suitable assumptions may be made and disclosed by way of a note.

Working notes should form part of the answers.

Time Allowed – 4 Hours **Maximum Marks – 100**

CASE STUDY 1

Skywalk Ltd. is a group established in Europe having diversified business interest. It maintains its records and financial statements under International Financial Reporting Standards.

The Board of Directors of the company hired your firm of Chartered Accountants to assist in closure of Financial Statements under IFRS as at 31st December 20X1. While commencing the exercise you find that there are certain transactions which need to be addressed considering the provisions of IFRS.

One of the divisions of Skywalk Ltd. is related to Travel across Europe, Asia Pacific and Australia. On 1st September, 20X1 it acquired Travelport Ltd. a popular travel company in Australia. Travelport Ltd. runs its bus coaches across Australia connecting tourists to Great Ocean Road from Melbourne and Blue Mountains from Sydney.

The summarized Statement of Financial Position of Travelport Ltd. at fair value on 1st September, 20X1 is as follows:

	₹ ’000
Goodwill	120
Operating licence	720
Bus terminal and rest rooms	180
Tow trucks	180
Bus coaches (4 nos)	600
Total	1,800

Travelport Ltd. has recently renewed its operating licence for ten years. It is recorded at its renewal cost. The carrying values of the property and tow trucks are stated at their estimated replacement cost. The bus coaches are valued at net selling price.

Two of the coaches fell off the cliff on 1st October 20X1 in a road accident on Great Ocean Road. This destroyed the two buses completely. The buses did not have any passengers on board as they were returning after routine servicing. Luckily the drivers managed to escape.

However, there was no way the coaches could be repaired and brought back to become road worthy for business again. This affected the Travelport’s business which was valued at this date at an estimated ₹ 1.2 million. The other two buses had a recoverable value at least equal to the cost on 1st October 20X1 and 31st December 20X1.

After this incident the brand image of Travelport Ltd. receded, and the number of passengers fell considerably – even below the expected reduced capacity. The tourists felt they could not rely on the drivers of Travelport Ltd.

Therefore, the business value was reassessed on 31st December 20X1 at ₹ 1.08 million. On the same day Skywalk Ltd. obtained an offer of ₹ 540,000 for the licence.

On 31st August, 20X1, the directors decided *on closure of a business division* in Europe which did not fit into its future vision and business strategy. The closure commenced on 5th October 20X1 and was due to be completed on 31st December 20X1. On 6th September 20X1, letters were sent to relevant employees offering voluntary redundancy or redeployment in other sectors of the business.

On 13th September, 20X1, negotiations commenced with relevant parties with a view to terminating existing contracts of the business segment and arranging sales of its assets. Latest estimates of the financial implications of the closure are as follows:

(i) Redundancy costs will total ₹ 30 million, excluding the payment referred to in (ii) below.

(ii) The pension plan (a defined benefit plan) will make a lump sum payment totaling ₹ 8 million to the employees who accept voluntary redundancy for termination of their rights under the plan. Skywalk Ltd. will pay this amount into the plan on 31st January 20X2.

The actuaries have advised that the accumulated pension rights that this payment will extinguish have a present value of ₹ 7 million and this sum is unlikely to alter significantly before 31st January 20X2.

(iii) The cost of redeploying and retraining staff who do not accept redundancy will total ₹ 6 million.

(iv) The business segment operates out of a leasehold property that has an unexpired lease term of 10 years from 1st January 20X1. The annual lease rentals on this property are ₹ 1 million, payable on 31st December in arrears. Negotiations with the owner of the property indicate that the owner would accept a single payment of ₹ 5·5 million in return for early termination of the lease.

There are no realistic opportunities for Skywalk Ltd. to sub-let this property. An appropriate rate to use in any discounting calculations is 10% per annum. The present value of an annuity of ₹ 1 receivable annually at the end of years 1 to 10 inclusive using a discount rate of 10% is ₹ 6.14.

(v) Plant having a net book value of ₹ 11 million at 31st December 20X1 will be sold for ₹ 2 million.

(vi) The operating losses of the business segment for January, February and March 20X2 are estimated at ₹ 10 million.

Your assistant is unsure of the extent to which the above transactions create liabilities that should be recognized as a closure provision in the financial statements as at 31st December 20X1. He is also unsure as to whether or not the results of the business segment that is being closed need to be shown separately.

On 1st April, 20X1, Skywalk Ltd. commenced project developing a new production technique in one of its business entities that would significantly reduce wastage. A team of 50 staff were employed on the project and the total annual salary cost of this team was ₹ 2 million accruing evenly during the year.

Other direct costs of the design and testing of the new technique were ₹ 2,00,000 p.m from 1st April, 20X1 to 31st December, 20X1 and ₹ 1,00,000 p.m. in January, February and March 20X2.

By 30th June 20X1 the team has developed an initial proposal and the technique was refined over the next six months, being subject to rigorous field testing. This testing was completed on 31st December, 20X1 and the new production technique was approved as being technically feasible and commercially viable from that date.

It was decided that the new production technique would be brought to practical use from 1st July, 20X2. On 31st December, 20X1, the directors estimated that the present value of the potential future cost savings the technique would generate were approximately ₹ 5 million.

On 1st October 20X1, Skywalk Ltd. signed a contract to purchase a machine from a foreign supplier on 31st March 20X2.

The purchase price of the machine, payable in cash on 31st March 20X2, was USD 2 million. On 1st October 20X1, Skywalk Ltd. entered into a forward contract to purchase USD 2 million on 31st March 20X2 for ₹ 140.0 million. On 31st December 20X1, a contract to buy USD 2 million on 31st March 20X2 would have required a payment of ₹ 150·0 million. On 31st March 20X2, the spot rate of exchange was ₹ 70 = USD 1. The forward contract was settled by the other party making a payment of ₹ 15 million to Skywalk Ltd. on that date.

Skywalk Ltd. estimated that the useful economic life of the machine was five years from 31st March 20X2, with no residual value. Skywalk Ltd. uses hedge accounting whenever permitted by IFRS 9. The currency contract fully complies with the criteria and conditions for hedge accounting as set out in IFRS 9.

Required:

Being a firm of chartered accountants, you are required to answer the following questions based on provisions of relevant IFRS:

I. Multiple Choice Questions

1. Show the amount to be recognized in balance sheet at 31st December 20X1 of property, plant and equipment for purchases of machine from foreign supplier.

    (a) ₹ 10 million

    (b) ₹ 140 million

    (c) ₹ 150 million

    (d) Nil

2. Calculate the gain on revaluation of the derivative for the year ended 31st December 20X2.

    (a) ₹ 5 million

    (b) ₹ 10 million

    (c) ₹ 15 million

    (d) ₹ 11.25 million

3. Calculate the net carrying amount of property, plant and equipment (machine purchased from foreign supplier) as at 31st December 20X2.

    (a) ₹ 119.00 million

    (b) ₹ 127.50 million

    (c) ₹ 106.25 million

    (d) ₹ 121.25 million

4. At which time the hedging instrument as derivative in this case is to be derecognized from books.

    (a) When the property, plant and equipment has been purchased

    (b) When the forward contract is settled

(c) When the company starts charging depreciation to property, plant and equipment

(d) At the end of relevant financial year when the contract is entered.

5. What are the characteristics of Derivatives?

(1) Value changes in response to changes in specified underlying price / index

(2) Requires no or little net investment

(3) Settled at a future date

(a) Only 1 & 3 are correct

(b) Only 1 & 2 are correct

(c) Only 2 & 3 are correct

(d) All 1, 2 & 3 are correct **(2 Marks each)**

II. Descriptive Questions

6. State the allocation of impairment losses and the valuation of each asset of Travelport Ltd. at 1st October 20X1 and 31st December 20X1 after impairment losses are recognized. **(6 Marks)**

7. Explain how the decision on *closure of a business division* should be reported in the financial statements of Skywalk Ltd. for the year ended 31st December 20X1. **(6 Marks)**

8. Comment how project developing a new production technique would be treated in financial statements of Skywalk Ltd. **(3 Marks)**

CASE STUDY 2

M. Chinnaswamy & Brothers Ltd. is company that is engaged in growing and maintaining coconut palms and selling the output in various forms. The company has a farmland having 2,00,000 coconut palms in the coastal area of Karnataka near Mangalore.

The company has adopted IFRS for the first time in financial year 20X3-20X4 including the standard of agriculture since the basic activities of the company are agricultural in nature.

The fair value of each coconut palm is derived based on the average realisable price of ₹ 30 per fruit. Each coconut palm grows 80 nuts per annum on an average basis. Each coconut palm can generate revenue for as long as 80 years and the current palms are only 20 year old. The management thinks that considering the risk factors in business the valuation of each palm can be considered at 5 times its annual revenue.

Although the company was primarily in agricultural activities until 20X1, it has taken major steps for forward integration to capture the higher pie of the value chain. Right from the coconut shells to the outer layer of the mature coconut which can be used to make coco pit – each item emanating from the palms and the nuts was carefully monitored and tracked by the company from 1st April 20X2.

During financial year 20X4-20X5, the company also did impressive work in Coconut shells division which made various utility items like key chains, cutlery and toys from the shells which were previously sold as scrap at a very negligible price. From the shells alone the company earned a revenue of ₹ 2.16 crore during the year with a net margin of 19%.

The following business divisions of the company were visible from the segment reporting presented in the annual report of financial year 20X4-20X5:

Business Segment	**Brief description**	**Segment revenue (₹ in crore)**
Coconut Oil	Sold across South India under the brand name – **CocoJar** (as hair oil only)	11.31
Copra	Sold to APMC yards as part of Spices	10.06
Tender Coconut	Sold as tender coconut water and tender coconut ice cream at Corporate canteens and retail outlets under the brand name – **Refresh!**	5.03
Sweets & Cookies	Coconut-based sweets and cookies sold as packed-food items under the brand name – **KaaiBella**	10.07

The sweets and cookies business has been growing at times every month from November, 20X4 to April 20X5. This propelled the thought process of the board and the company decided to divert more resources to this division with an investment of additional ₹ 10 crore (non-current assets) with immediate effect from 1st May, 20X5. The carrying amount of investment in PPE already made for this division as on 31st March 20X5 was ₹ 5.16 crore. The segment related old liability as on 31st March 20X6 was ₹ 2.13 crore. The fresh bank loan for the ₹ 10 crore investment was ₹ 7 crore of which ₹ 6.51 crore was outstanding as on 31st March 20X6. The carrying amount of freshly acquired assets was ₹ 6.85 crore as on 31st March 20X6.

Investment in Tender Coconut outlets and factory set for productions units was ₹ 6 crore with the carrying amount of ₹ 5.37 crore as on 31st March 20X6 and segment related liability of ₹ 2.12 crore on the same date.

During August 20X5, the Ooty Hotels Association (OHA) chairman and his team visited the corporate office of the company at Mangalore. The deal was to supply tender coconuts to Ooty Hotels at an agreed price throughout the year. The agreement came into effect from 1st September 20X5 whereby the company shall reserve 15,000 coconut palms for OHA and will charge a concessional rate of ₹ 15 only per nut supplied to OHA. OHA will in turn supply the tender coconuts to each Ooty Hotel at the same price. OHA will also market the company's sweets and cookies through each member hotel of OHA. This contract price is applicable irrespective of the ownership of palm trees (it is not an entity-specific restriction).

The response for KaaiBella brand has been overwhelming for the company. Similarly, the shells business has also grown beyond estimates during financial year 20X5-20X6.

Keeping the growth in mind, the management has decided to build another farmland with 50,000 new coconut palms. The cost of the land purchased for the same is ₹ 50 crore and the cost of baby palms was ₹ 50 per piece. In addition, the company has to incur ₹ 5.5 lacs p.m. from the date of cultivation for the maintenance and nutrition of the palms for 10 years until they are fully grown and start yielding fruits. The land was purchased and put to use on 1st July 20X5 and activity of planting the baby palms was complete within 5 days. Bank loan for this entire deal was negotiated as "Coconut Palm area" and not just a land. The project gestation period was shown as 10 years. Since no bank would wait for 10 years to start getting the EMIs the bank had agreed to start the repayment from year 3 onwards – from the existing financial resources of the company. Bank loan for this project was ₹ 40 crore at a rate of 10% p.a. Interest will start accumulating from day 1 and will be added to the principal amount every year for two years and the EMI will start from year 3 on the amount so accumulated.

The new coconut palm will be used exclusively for the captive consumption of the company.

For the financial year 20X5-20X6 the revenue numbers have changed significantly for the company due to forward integration and expansion plans over the last 5 years. The following information is available:

Keeping aside the 15,000 palms for OHA contract, the company utilised the remaining palms in the following manner –

Coconut Oil – 33%, Copra – 30%, Sweets & Cookies – 10%, Tender Coconut – 19.50%

Revenue from Coconut oil and Copra segments was ₹ 13.33 crore and ₹ 5.06 respectively.

The Sweets & Cookies segment sold 20.72 lacs kg items at an average price of ₹ 240 per kg. The tender coconut segment which is entirely run and managed by the company (no franchise) realised an average price of ₹ 40 per coconut.

The shells business had an average realisation of ₹ 30 per shell* in revenue. Coco pit produced from the outer layer of the shell was sold 20 lacs kg in quantity which fetched an average rate of ₹ 8 per kg. Coco pit is used in hydroponic farming and nurseries.

***Note:** OHA did not commit to return the coconut shells to company since it's difficult to implement the return scheme, keeping watch on the same.

I. Multiple Choice Questions

Choose the best option from the given choices for each of the question or statement below:

1. Accounting treatment of coconut palms in the farm is covered in ______ and not in ______.

   (a) IAS 41 'Agriculture'; IAS 16 'Property Plant & Equipment'

   (b) IAS 16 'Property Plant & Equipment'; IAS 41 'Agriculture'

   (c) IAS 41 'Agriculture'; IAS 40 'Investment Properties'

   (d) IAS 40 'Investment Properties'; IAS 41 'Agriculture'.

2. The contract between Ooty Hotels Association (OHA) and the company provides a clue for fair valuation of coconut palms. The valuation of 2 Lac coconut palms in the company's farm can be done at ____________ for the quarter ended 30th September 20X5.

   (a) ₹ 120 crore

   (b) ₹ 222 crore

   (c) ₹ 240 crore

   (d) ₹ 231 crore

3. Which of the following statements is correct?

   I. Tender coconuts sold to OHA is an agricultural produce.

   II. Copra sold to wholesale dealers of spices is an agricultural produce.

   III. Ripe coconut with shells (outer layer peeled) sold to APMC yards is not an agricultural produce.

   (a) Statement I only

   (b) Statement II only

(c) Statement I & II

(d) Statement I & III

4. The interest cost in respect of loan taken for the cultivation of 50,000 new coconut palms must be capitalised since the bearer plants are expected to be put to use only after 2030.

   Which of the following is correct?

   (a) The above statement is false. Since bearer plants are valued at fair value less costs to sell, interest can't be capitalised.

   (b) The above statement is false. Although bearer plants are a part of Property, Plant and Equipment, borrowing cost needs to be expensed for such plants.

   (c) The above statement is true. Borrowing cost must be capitalised as part of the cost of bearer plants.

   (d) The above statement is false. Bearer plants are carried at cost of purchase only.

5. Which of the following is not a reportable business segment, based on revenue criteria, for the company for financial year 20X5-20X6?

   (a) Coco shells

   (b) Coconut oil

   (c) Copra

   (d) Tender coconut **(2 Marks each)**

II. Descriptive Questions

1. Prepare a note for the purpose of disclosure in accordance with IAS 41 for the biological assets of the company. Calculation of amounts should form part of your answers. All disclosures are to be made for the year ended 31st March 20X6. **(6 Marks)**

2. Calculate revenue of the company for the financial year 20X5-20X6. Make a separate list of reportable business segments with segment revenue along with segment assets and liabilities, if possible. The coconut palm as such does not belong to any particular segment as on 31st March 20X6. **(6 Marks)**

3. Show detailed computation of borrowing cost that needs to be capitalized as part of the cost of bearer plants to be held as biological assets of the company pertaining to new 50,000 coconut palms for the year ended 31st March 20X6. Also, make suitable disclosures as per IAS 23 as on 31st March 20X6. **(3 Marks)**

CASE STUDY 3

You are the Financial Controller of Blueberry Ltd. Your assistant is preparing the first draft of the financial statements for the year ended 30th September 20X3. He has a reasonable general accounting knowledge but is not familiar with the detailed requirements of all relevant international financial reporting standards. Your assistant requires your advice and he has sent you a memorandum.

On 1st October 20X2, Blueberry Ltd lent ₹ 2 million to a customer in order to assist them with their expansion plans. The loan cost the company ₹ 1,00,000 to arrange. Your assistant is not clear whether we need to charge ₹ 1,00,000 as a cost in the current year. The directors agreed not to charge interest on this loan to help the customer's short-term cash flow but expected the customer to repay ₹ 2·4 million on 30th September 20X4.

This will mean the Company cannot take any profit this year but there will be a bonus next year when the payment is received. According to the finance department the effective annual rate of interest on this loan is 6·9%. Your assistant does not understand the relevance of this information as no interest is payable.

Just before the year end, we heard from the customer that the poor economic climate has caused them significant problems and in order to help them we agreed to reduce the amount repayable by them on 30th September 20X4 to ₹ 2·2 million. Please advise treatment for the year ended 30th September 20X3.

On 1st October, 20X2 the board of Blueberry Ltd granted key employees share options that are subject to vesting conditions. Details of the award are as follows:

(i) 50 employees can potentially receive 5,000 options each on 30th September 20X4. The options that vest (see below) will allow the employees to purchase shares in Blueberry Ltd at any time in the year to 30th September 20X5 for ₹ 15 per share. The par (or nominal) value of the shares is ₹ 1 per share.

(ii) The options only vest if the employees remain as employees of Blueberry Ltd until 30th September 20X4 if the share price of Blueberry Ltd is at least ₹ 20 by that date.

(iii) On 1st October, 20X2 the board of Blueberry Ltd estimated that five of the 50 employees would leave in the following two years. Three of the employees left in the year ended 30th September 20X3 and at that date the board considered that a further three would leave in the year to 30th September 20X4.

(iv) On 1st October, 20X2 the share price of Blueberry Ltd was ₹ 15. The price had risen to ₹ 18 by 30th September, 20X3 and the directors are reasonably confident that the price will exceed ₹ 20 by 30th September 20X4.

(v) On 1st October 20X2 the directors estimated that the fair value of each of the granted options was ₹ 4·50. This estimate had risen to ₹ 5 by 30th September 20X3.

The directors want to know the likely impact of the transactions mentioned above on the financial statements of future years under the following assumptions:

- The directors' estimates about the number of relevant employees who will leave during the year ended 30th September 20X4 will be accurate.
- The employees will exercise their options in 90% of cases during the year ended 30th September 20X4 and the unexercised options will lapse on 30th September 20X5.

On 1st April 20X3, Blueberry Ltd decided to dispose of a business component. This business component is a disposal group that satisfied the criteria for classification as held for sale at 1st April 20X3.

The carrying values of the relevant assets and liabilities of the component in the financial statements of Blueberry Ltd on 1st April 20X3, measured individually in accordance with applicable International Financial Reporting Standards were as under:

Particulars	Amount ₹ '000
Goodwill	10,000
Property, plant and equipment – estimated future useful economic life 4 years	25,000
Net current assets	5,000
Total	40,000

On 1st April 20X3, the directors estimated that the fair value less costs to sell of this disposal group was ₹ 28 million. The group was disposed of on 31st October 20X3 for ₹ 31 million. This was in line with a revised estimate made on 30th September 20X3.

The profit after tax of the business component for the year ended 30th September 20X3 was ₹ 3 million.

On 1st October 20X2, Blueberry Ltd acquired control of Armstrong Ltd, purchasing 60% of its issued ordinary share capital. Armstrong Ltd is located in a country where compliance with IFRS is required by law.

In that country, there is no requirement to discount liabilities. No material fair value adjustments were identified at the date of acquisition of Armstrong Ltd, except in respect of a deferred liability to a supplier which will fall due on 1st October 20X4. The amount payable on that date will be ₹ 3,00,000. The discount rate relevant to the liability is 8%.

Armstrong Ltd.'s profit for the period ended 30th September, 20X3 was ₹ 67,600 before taking into account any unwinding of the discount in respect of the liability referred to above.

Blueberry Ltd entered into the following transactions during the year ended 30th September, 20X3:

(a) Entered into a speculative interest rate option costing ₹ 10,000 on 1st October 20X3 to borrow ₹ 60,00,000 from Exon Bank commencing 31st December 20X3 for 6 months at 4%. The value of the option at 30th September 20X3 was ₹ 15,250.

(b) Purchased 6% debentures in Fox Ltd on 1st October 20X2 (their issue date) for ₹ 1,50,000 as an investment. Blueberry Ltd intends to hold the debentures until their redemption at a premium in 5 years' time. The effective rate of interest is 8%.

(c) Purchased 50,000 shares in Cox Ltd on 1st April 20X3 for ₹ 3.50 each as an investment. The share price on 30th September 20X3 was ₹ 3.75.

Blueberry Ltd only designates financial assets as at fair value through Profit or loss where this is unavoidable.

I. Multiple Choice Questions

1. For financial assets classified as bonds, how are unrealized gains and losses reflected in shareholders' equity?

   (a) They are not recognized

   (b) Shown as an adjustment in paid-in capital

   (c) Recognized as amortized cost and measured through effective interest method

   (d) None of the above.

2. What will be the impact of the options on the Statement of Profit & Loss of Blueberry Ltd for the year ended 30th September 20X5? Ignore deferred taxation.

   (a) Expense-₹ 4,95,000

   (b) Gain- ₹ 99,000

   (c) Loss- ₹ 99,000

   (d) None of the above

3. How much expenses is to be recognized in the financial statements for the year ended 30th September 20X3 on transactions related to financial instruments?

   (a) Loss- ₹ 15,250

   (b) Gain- ₹ 5,250

   (c) Loss- ₹ 17,250

   (d) Gain- ₹ 17,250

4. With respect to Blueberry Ltd acquisition of Armstrong Ltd, calculate the share of profit for the period attributable to equity shareholders of the parent, after taking into account any adjustment required in respect of the liability.

   (a) ₹ 28,140

   (b) ₹ 46,900

   (c) ₹ 18,760

   (d) ₹ 67,600

5. With respect to Blueberry Ltd acquisition of Armstrong Ltd, calculate expense with respect to transaction, if any for the period ended 30th September 20X3.

   (a) ₹ 22,200

   (b) ₹ 24,000

   (c) ₹ 20,700

   (d) Nil

II. Descriptive Questions:

6. How would the loan given to the customer be regarded? Discuss the treatment under the provisions related to the relevant IFRS. **(3 Marks)**

7. Explain the impact of granting the options to employees in the Statement of Profit & Loss of Blueberry Ltd for the year ended 30th September 20X3 and on the Statement of Financial Position of Blueberry Ltd as at 30th September 20X3. Ignore deferred taxation.

   Also discuss the impact of the assumptions mentioned in the case study above regarding the options on the Statement of Profit & Loss of Blueberry Ltd for the years ended 30th September 20X4 and 20X5 and on the Statement of Financial Position of Blueberry Ltd as at 30th September 20X4 and 20X5. Ignore deferred taxation. **(5 Marks)**

8. With respect to disposal of a business component, compute the carrying amount of the goodwill and property, plant and equipment of the business component on 1st April 20X3 immediately after classification as held for sale.

   Also compute the carrying amount of the goodwill and property, plant and equipment of the business component on 30th September 20X3 and show the minimum amounts that must be presented on the face of the statement of comprehensive income of Blueberry Ltd for the year ended 30th September 20X3 concerning the business component. **(5 Marks)**

9. Discuss the accounting treatment and present the relevant extracts from the financial statements for the year ended 30th September 20X3 on transactions related to financial instruments.

   (2 Marks)

CASE STUDY 4

Monsoon Limited is engaged in various businesses. One of the business is of manufacturing sugar and chemicals. The Company has taken a term loan for ₹ 5 crores from State Bank to buy certain plant and machinery during the year ended 31 March 20X2. The loan is repayable over a period of 5 years. The terms and conditions of the loan agreement requires the company to maintain a current ratio of 1.33 : 1 and debt-equity ratio of 1 : 2. If these loan covenants fall below this level, then the bank has a right to recall the entire loan.

The Loan outstanding as on 31 March, 20X3 was ₹ 4.25 crores. The current ratio of Monsoon Limited was 1 : 1 and debt equity ratio was 0.5 : 2. State Bank has sent a notice on 5 April 20X3 demanding repayment of loan, on account of breach of terms of the loan agreement. The financials were signed on 10 May, 20X3.

On receiving the notice, the CFO of Monsoon Limited negotiated with the bank and ensured to rectify the breach. As a result, on 25 April, 20X3, the Bank has agreed not to recall the loan and allowed the Company to achieve the contracted current and debt-equity ratio by 20X5.

Monsoon Limited has adopted revaluation model since 1 April, 20X1 to measure one of its class of Property plant and equipment (PPE) and have revalued the PPE as follows:

(i) As on 1 April, 20X1–PPE has been revalued up by ₹ 3,00,000.

(ii) As on 31 March, 20X2–PPE has been revalued down by ₹ 3,60,000

(iii) As on 31 March, 20X3–PPE has been revalued up by ₹ 5,00,000

During the year 20X2-20X3, Monsoon Limited bought a private jet for the use of its top ranking officials. The cost of the private jet is ₹ 15 crores and has a composite useful life of 9 years. The engine of the jet has a useful life of 7 years. The private jet's tyres are replaced every 3 years. The Company is following straight line method of depreciation.

Monsoon Limited acquired, on 30 September, 20X2, 70% of the share capital of Mark Limited, an entity registered as company in Germany. The functional currency of Monsoon Limited is ₹ and its financial year end is 31 March, 20X3.

The fair value of the net assets of Mark Limited was 23 million EURO and the purchase consideration paid is 17.5 million EURO on 30 September, 20X2.

The exchange rates as on 30 September, 20X2 was 82 ₹/EURO and at 31 March, 20X3 was 84 ₹/EURO.

Mark Limited sold goods costing 2.4 million EURO to Monsoon Limited for 4.2 million EURO during the year ended 31 March 20X3. The exchange rate on the date of purchase by Monsoon Limited was 83 ₹/EURO. The entire goods purchased from Mark Limited are unsold as on 31 March 20X3.

Monsoon Limited is undertaking reorganization. Under the plan, part of the entity's business will be demerged and will be transferred to a separate entity, Season Limited. This also will involve a transfer of part of the pension obligation to Season Limited. Due to this, Season Limited will have a deductible temporary difference for the year ended 31 March 20X3. It is anticipated that Season Limited will be loss making for the first eleven years of its existence, but thereafter it will become a profitable entity. The future forecasted profit is based on estimates of sales to inter-group companies.

Monsoon Limited also has a subsidiary in USA, which adopted US GAAP. It has valued its inventory under LIFO method for Income Tax purposes.

Monsoon Limited holds some vacant Land for which the use is not yet determined. The Land is situated in a prominent area of the city where lot of commercial complexes are coming up and there is no legal restriction to convert the land into a commercial land. The Company is not interested in development the land to a commercial complex as it is not its business objective. Currently the land has been let out as a parking lot for the commercial complexes around. The Company has classified the above property as investment property.

Monsoon Limited holds equity shares of a private company. In order to determine the fair value of the shares, the company used discounted cash flow method as there were no similar shares available in the market.

I. Multiple Choice Questions

1. How the long-term loan from State Bank has to be classified in the financials for the year ended 31st March 20X3 in case Monsoon Limited has not negotiated with the bank for rectification of breach?

   (a) Other current liabilities

   (b) Current financial liability

   (c) Non-current financial liability

   (d) Other non-current liability

2. After negotiation with State Bank, how the long-term loan has to be classified in the financials for the year ended 31 March 20X3?

   (a) Other current liabilities

   (b) Current financial liability

   (c) Non-current financial liability

   (d) Other non-current liability

3. With reference to usage of revaluation model to class of PPE, how will the increase in year 20X2-20X3 be recognized in the financials of Monsoon Limited?

   (a) ₹ 5,00,000 is credited to other comprehensive income.

   (b) ₹ 60,000 is credited to profit and loss account and ₹ 4,40,000 is credited to other comprehensive income.

   (c) ₹ 60,000 is credited ton other comprehensive income and ₹ 4,40,000 is credited to profit and loss account.

   (d) ₹ 5,00,000 is credited to profit and loss account.

4. With respect to private jet purchased during the year 20X2-20X3, what is the useful life to be considered?

   (a) 9 years of composite useful life

   (b) 7 years useful life for the engine, 3 years useful life for the tyres, and 9 years useful life to be applied for the balance cost of the jet.

   (c) 3 years useful life, based on conservatism (the lowest useful life of all the parts of the jet).

   (d) 7 years useful life, based on simple average of useful lives of all major components of the jet.

5. What would be the useful life of the private jet for the purpose of depreciation if the said company is following US GAAP?

   (a) 9 years of composite useful life

(b) 7 years useful life for the engine, 3 years useful life for the tyres, and 9 years useful life to be applied for the balance cost of the jet.

(c) 3 years useful life, based on conservatism (the lowest useful life of all the part of the jet).

(d) 7 years useful life, based on simple average of useful lives of all major components of the jet.

(2 Marks each)

II. Descriptive Questions

6. (i) On acquisition of Mark limited, what is the value at which the goodwill / capital reserve has to be recognized in the financial statements of Monsoon Limited as on 31 March 20X3?

(2 Marks)

(ii) Determine the unrealized profit to be eliminated in the preparation of consolidated financial statements of Monsoon Limited and Mark Ltd. **(2 Marks)**

7. Should Season Limited recognize the deductible temporary difference as a deferred tax asset?

(3 Marks)

8. Discuss the implication of adopting of US GAAP by a subsidiary in USA, both from the point of view of US GAAP and also from the point of view of its consolidation with the parent company which follows IFRS. **(2 Marks)**

9. What would be the fair value of the land for the purpose of disclosure under IFRS. Also state that on what basis will the land be fair valued under IFRS? **(3 Marks)**

10. Determine under which level of fair value hierarchy does 'discounted cash flow method' will fall? What will be your answer if the quoted price of similar companies were available and can be used for fair valuation of the shares. **(3 Marks)**

CASE STUDY 5

Free Bird Limited, is currently engaged in different business segments and is also looking to expand its operations. The Company is also exploring investment from an overseas investor to carry out the expansion plan. During the month of April 20X4, an overseas investor showed interest to acquire 51% stake in Free Bird Limited and has appointed an independent consultant to carry out the due diligence of Free Bird Limited. As per one of the conditions of Memorandum of Understanding (MoU), the Company is required to submit its financial statements for the year ended 31st March, 20X4 as per IFRS.

Free Bird Limited is in the process of computation of the deferred taxes as per applicable IFRS and wants guidance on the tax treatment for the following:

The Company had acquired 40% in GK Limited for an aggregate amount of ₹ 45 crore. The shareholding gives Free Bird Limited significant influence over GK Limited but not control and therefore the said interest in GK Limited is accounted using the equity method. Under the equity method, the carrying value of investment in GK Limited was ₹ 70 crore on 31st March, 20X3 and ₹ 75 crore as on 31st March, 20X4. As per the applicable tax laws, profits recognised under the equity method are taxed if and when they are distributed as dividend or the relevant investment is disposed of. Consider tax rate of 20%.

The Company measures its head office property using the revaluation model. The property is revalued every year as on 31 March. On 31 March 20X3, the carrying value of the property (after revaluation) was

₹ 40 crore whereas its tax base was ₹ 22 crore. Carrying amount of property in the books of the company on 31 March 20X3 was equal to the carrying amount of the property as per tax records. During the year ended 31 March 20X4, the Company charged depreciation in its Statement of Profit or Loss of ₹ 2 crore and claimed a tax deduction for tax depreciation of ₹ 1.25 crore. On 31 March 20X4, the property was revalued to ₹ 45 crore. As per the tax laws, the revaluation of Property, Plant & Equipment does not affect taxable income at the time of revaluation. Consider tax rate at 20%.

During the year, Free Bird Limited delivered manufactured products to customer K. The products were faulty and on 1 October 20X3 customer K commenced legal action against the Company claiming damages in respect of losses due to the supply of faulty product. Upon investigating the matter, Free Bird Limited discovered that the products were faulty due to defective raw material procured from supplier F. Therefore, on 1 December 20X3, the Company commenced legal action against F claiming damages in respect of the supply of defective raw materials.

Free Bird Limited has estimated that it's probability of success of both legal actions, the action of K against Free Bird Limited and action of Free Bird Limited against F, is very high.

On 1 October 20X3, Free Bird Limited has estimated that the damages it would have to pay K would be ₹ 5 crore. This estimate was revised to ₹ 5.2 crore as on 31 March 20X4 and ₹ 5.25 crore as at 15 May 20X4. This case was eventually settled on 1 June 20X4, when the Company paid damages of ₹ 5.3 crore to K.

On 1 December 20X3, Free Bird Limited had estimated that it would receive damages of ₹ 3.5 crore from F. This estimate was revised to ₹ 3.6 crore as at 31 March 20X4 and ₹ 3.7 crore as on 15 May 20X4. This case was eventually settled on 1 June 20X4 when F paid ₹ 3.75 crore to Free Bird Limited. Free Bird Limited in its financial statements for the year ended 31 March 20X4, provided ₹ 3.6 crore. The financial statements were authorised by the Board of Directors on 26 April 20X4.

On 1 April 20X3, Free Bird Limited purchased 10 lakh options to acquire shares in KS Ltd., a listed entity. The Company paid ₹ 0.25 per option which allows the Company to purchase shares in KS Ltd. for a price of ₹ 2 per share. The exercise date for the option was 31 December 20X3. On 31 December 20X3, when the market value of a share in KS Ltd. was ₹ 2.6 per share, the Company exercised all its options to acquire shares in KS Ltd.

In addition to the purchase price, the Company has also incurred directly attributable cost of ₹ 1 lakh for purchase of 10 lakh shares in KS Ltd. The Company has classified these shares as trading portfolio. However, the Company has not disposed of any of the shares in KS Ltd. between 31 December 20X3 to 31 March 20X4.

The market value of the shares of KS Ltd. as on 31 March 20X4 is ₹ 2.90 per share.

Free Bird Limited acquired 100% of Coal Private Limited, on 1 January 20X3. The fair value of the purchase consideration was ₹ 10 crore consisting of ordinary shares of ₹ 100 each of Free Bird Limited. The fair value of the net assets acquired was ₹ 7.5 crore. At the time of the acquisition, the value of the ordinary shares of Free Bird Limited and the net assets of Coal were only provisionally determined. On 30 November 20X3 it was finally determined that the fair value of Free Bird Limited's shares was ₹ 11 crore and the fair value of net assets of Coal was ₹ 8 crore. However, the directors of Free Bird Limited have seen the fair value of the company's shares decline since 1 January 20X3 and wanted to adopt the fair value of the shares as of 1 February 20X4, which will result in the fair value of consideration being valued at ₹ 9 crore.

One of the subsidiaries of Free Bird Limited started its business in India with Indian Rupee as its functional currency. After several years, the entity expanded and started exporting its product to Europe. During the year ended 31 March 20X3 only 30% of the business was conducted in Euro. By the end of 31 March

20X4, 90% of the business was conducted with Europe and the transaction were denominated in Euro. The raw materials required (for the products to be exported to Europe) are all imported materials and the purchase transactions are denominated in Euro.

Free Bird Limited has constructed a mall earlier. A portion of a mall is renovated by constructing a food court, spa and gaming zone so as to increase the footfalls in the mall. The food court and gaming zone are expected to result in a significant increase in sales for the shops and outlets of the mall.

Free Bird Limited previously had a defined pension plan (a defined benefit pan) under which the employees who joined before 1 April 20X0 were enrolled. With respect to employees who joined on or after 1 April 20X0 were all enrolled in the industrial pension plan. The Company found that the industrial pension plan was more beneficial to the employees than the defined pension plan. Hence, during 20X3-20X4 it decided to shift all the employees from defined pension plan to the industrial pension plan. The entity paid ₹ 5 crore to the employees who in turn agreed to forfeit the pension entitlement from the defined pension plan. The liability recognised in the financials, for the year ended 31 March 20X3, with respect to the pension liability was ₹ 7 crore.

You being the consultant of the company and having expertise in IFRS, are required to guide on accounting treatment of the abovementioned issues.

I. Multiple Choice Questions

1. What is the value of purchase consideration and fair value of net assets of Coal Private Limited as at the date of acquisition?

   (a) Purchase consideration ₹ 11 crore, net asset value ₹ 8 crore.

   (b) Purchase consideration ₹ 10 crore, net asset value ₹ 7.5 crore.

   (c) Purchase consideration ₹ 9 crore, net asset value ₹ 8 crore.

   (d) Purchase consideration ₹ 11 crore, net asset value ₹ 7.5 crore.

2. What will be the functional currency of the subsidiary of Free Bird Limited for the year 20X3-20X4?

   (a) Changed to Euro at the end of financial year 20X3-20X4, if it is considered that the underlying transactions, events and conditions of business have changed.

   (b) Changed to Euro at the beginning of financial year 20X3-20X4, if it is considered that the underlying transactions, events and conditions of business have changed.

   (c) Changed to Euro at the end of financial year 20X2-20X3, if it is considered that the underlying transactions, events and conditions of business have changed.

   (d) The functional currency remains to be Indian Rupee.

3. What should be the accounting treatment for the cost incurred for the renovation?

   (a) Expenses incurred for food court and gaming zone should be charged to statement of profit or loss;

   (b) Expenses incurred for food court, spa and gaming zone should be charged to statement of profit or loss;

   (c) Expenses incurred for food court, spa and gaming should be capitalised;

   (d) Expenses incurred for food court and gaming should be capitalised.

4. What is the entry to be passed in the books of account as on 31 March 20X4 with respect to legal action commenced by customer K on the company?

(a)	Statement of Profit or Loss A/c	Dr.	₹ 5.2 crore	
	To Current Liability A/c			₹ 5.2 crore
(b)	Statement of Profit or Loss A/c	Dr.	₹ 5.3 crore	
	To Non-Current Liability A/c			₹ 5.3 crore
(c)	Statement of Profit or Loss A/c	Dr.	₹ 5.25 crore	
	To Current Liability A/c			₹ 5.25 crore
(d)	Other Comprehensive Income A/c	Dr.	₹ 5.2 crore	
	To Current Liability A/c			₹ 5.2 crore

5. What will the accounting treatment of the action of Free Bird Limited against supplier F as per applicable IFRS?

(a) Asset receivable shall be recognised for ₹ 3.75 crore

(b) Asset receivable shall be recognised for ₹ 3.70 crore

(c) Asset receivable shall be recognised for ₹ 3.60 crore

(d) It will be considered as contingent assed which will not be recognised in the books.

(2 Marks each)

II. Descriptive Questions

6. How should this be accounted in the financials for the year ended 31 March 20X4? **(2 Marks)**

7. With respect to GK Limited, what will be the deferred tax and where will it be impacted? **(2 Marks)**

8. Compute the deferred tax liability as on 31 March 20X4 and the charge/credit to the Statement of Profit or Loss and / or Other Comprehensive Income on head office property. **(6 Marks)**

9. The Company has requested you to suggest the accounting treatment of the above arrangement and transaction of acquisition of shares in KS Ltd. **(5 Marks)**