# MOCK TEST PAPER 2

## FINAL (NEW) COURSE: GROUP – I

## PAPER – 1: FINANCIAL REPORTING

***Question No.1 is compulsory. Candidates are required to answer any four questions from the remaining five questions.***

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

*Working notes should form part of the answers.*

**Time Allowed – 3 Hours** **Maximum Marks – 100**

1. (a) Master Creator Private Limited (a subsidiary of listed company) is an Indian company to whom Ind AS are applicable. Following draft balance sheet is prepared by the accountant for year ending 31st March 20X2.

**Balance Sheet of Master Creator Private Limited as at 31st March, 20X2**

| Particulars | Rs. |
|---|---|
| **ASSETS** | |
| **Non-current assets** | |
| Property, plant and equipment | 85,37,500 |
| Financial assets | |
| Other financial assets (Security deposits) | 4,62,500 |
| Other non-current assets (capital advances) | 17,33,480 |
| Deferred tax assets | 2,54,150 |
| **Current assets** | |
| Trade receivables | 7,25,000 |
| Inventories | 5,98,050 |
| Financial assets | |
| Investments | 55,000 |
| Other financial assets | 2,17,370 |
| Cash and cash equivalents | 1,16,950 |
| **TOTAL ASSETS** | **1,27,00,000** |
| **EQUITY AND LIABILITIES** | |
| Equity share capital | 10,00,000 |
| **Non-current liabilities** | |
| Other Equity | 25,00,150 |
| Deferred tax liability | 4,74,850 |
| Borrowings | 64,00,000 |
| Long term provisions | 5,24,436 |
| **Current liabilities** | |
| Financial liabilities | |
| Other financial liabilities | 2,00,564 |
| Trade payables | 6,69,180 |
| Current tax liabilities | 9,30,820 |
| **TOTAL EQUITY AND LIABILITIES** | **1,27,00,000** |

**Additional Information:**

1. On 1st April 20X1, 8% convertible loan with a nominal value of Rs. 64,00,000 was issued by the entity. It is redeemable on 31st March 20X5 also at par. Alternatively, it may be converted into equity shares on the basis of 100 new shares for each Rs. 200 worth of loan.

   An equivalent loan without the conversion option would have carried interest at 10%. Interest of Rs. 5,12,000 has already been paid and included as a finance cost.

   Present Value (PV) rates are as follows:

| Year End | @ 8% | @ 10% |
|---|---|---|
| 1 | 0.93 | 0.91 |
| 2 | 0.86 | 0.83 |
| 3 | 0.79 | 0.75 |
| 4 | 0.73 | 0.68 |

2. After the reporting period, the board of directors have recommended dividend of Rs. 50,000 for the year ending 31st March, 20X1. However, the same has not been yet accounted by the company in its financials.

3. 'Other current financial liabilities' consists of the following:

| Particulars | Amount (Rs.) |
|---|---|
| Wages payable | 21,890 |
| Salary payable | 61,845 |
| TDS payable | 81,265 |
| Interest accrued on trade payables | 35,564 |

4. Property, Plant and Equipment consists following items:

| Particulars | Amount (Rs.) | Remarks |
|---|---|---|
| Building | 37,50,250 | It is held for administration purposes |
| Land | 15,48,150 | It is held for capital appreciation |
| Vehicles | 12,37,500 | These are used as the conveyance for employees |
| Factory premises | 20,01,600 | The construction was started on 31st March 20X2 and consequently no depreciation has been charged on it. The construction activities will continue to happen, and it will take 2 years to complete and be available for use. |

5. The composition of 'other current financial assets' is as follows:

| Particulars | Amount (Rs.) |
|---|---|
| Interest accrued on bank deposits | 57,720 |
| Prepaid expenses | 90,000 |
| Royalty receivable from dealers | 69,650 |

6. Current Investments consist of securities held for trading which are carried at fair value through profit & loss. Investments were purchased on 1st January,20X2 at Rs.55,000 and accordingly are shown at cost as at 31st March 20X2. The fair value of said investments as on 31st March 20X2 is Rs.60,000.

7. Trade payables and Trade receivables are due within 12 months.

8. There has been no changes in equity share capital during the year.

9. Entity has the intention to set off a deferred tax asset against a deferred tax liability as they relate to income taxes levied by the same taxation authority and the entity has a legally enforceable right to set off taxes.

10. Other Equity consists retained earnings only. The opening balance of retained earnings was Rs.21,25,975 as at 1st April 20X1.

11. No dividend has been actually paid by company during the year.

12. Assume that the deferred tax impact, if any on account of above adjustments is correctly calculated in financials.

Being Finance & Accounts manager, you are required to identify the errors and misstatements if any in the balance sheet of Master Creator Private Limited and prepare corrected balance sheet with details on the face of the balance sheet i.e. no need to prepare notes to accounts, after considering the additional information. Provide necessary explanations/workings for the treated items, wherever necessary. **(16 Marks)**

(b) ABC Bank gave loans to a customer – Target Ltd. that carry fixed interest rate @ 10% per annum for a 5 year term and 12% per annum for a 3 year term. Additionally, the bank charges processing fees @1% of the principal amount borrowed. Target Ltd borrowed loans as follows:

- 10 lacs for a term of 5 years

- 8 lacs for a term of 3 years.

Compute the fair value upon initial recognition of the loan in books of Target Ltd. and how will loan processing fee be accounted? **(4 Marks)**

2 (a) Besides construction activity, Buildings & Co. Limited is also engaged in the trading of Copper. On 1st April, 20X1, it had 100 kg of copper costing Rs. 70 per kg - totalling Rs. 7000. The Company has a scheduled delivery of these 100 kgs of copper to its customer on 30th September, 20X1 at the rate of USD 100 on that date. To protect itself from decline in currency exchange rate (USD to Rs.), the entity hedges its position by entering into currency futures contract for equivalent currency units at Rs. 76 / USD. The future contract mature on 30th September, 20X1. The management performed an assessment of hedge effectiveness and concluded that the hedging relationship qualifies for cash flow hedge accounting. The entity determines and documents that changes in fair value of the currency futures contract will be highly effective in offsetting variability in cash flow of currency exchange. On 30th September, 20X1, the entity closes out its currency futures contract. On the same day, it also sells its inventory of copper at USD 100 when the spot rate is Rs. 72 / USD.

You are required to prepare detailed working and pass necessary journal entries for the sale of copper and the corresponding hedge instrument taken by the company. Pass the journal entries as on the initial date (i.e. 1st April 20X1), first quarter end reporting (i.e. 30th June 20X1) and date of sale of copper and settlement of forward contract (i.e. 30th September 20X1).

Assume the exchange rates as follows and yield @ 6% per annum.

| Date | Future price for 30th September 20X1 delivery (Rs. / USD) |
|---|---|
| 1st April, 20X1 | 76 |
| 30th June, 20X1 | 74 |
| 30th September, 20X1 | 71 |

**(10 Marks)**

(b) Buildings Limited entered into a 10-year lease for 6,000 square meter of office space. The annual lease payments are Rs. 60,000 payable at the end of each year. The interest rate implicit in the lease cannot be readily determined. Buildings Limited's incremental borrowing rate at the commencement date is 8% p.a. At the beginning of 6th year, Buildings Limited and lessor agree to amend the original lease to reduce the space to only 3,000 square meters of the original space starting from the end of the first quarter of year 6. The annual fixed lease payments (from year 6 to year 10) are Rs. 35,000. Buildings Limited's incremental borrowing rate at the beginning of year 6 is 6% p.a.

The CFO of the Company has requested your suggestion on how to account for the modification in the lease of office space? Prepare the detailed working for the modification. **(10 Marks)**

3. (a) The Balance Sheet of David Ltd. and Parker Ltd. as of 31st March, 20X1 is given below:

(Rs. in lakh)

| Assets | David Ltd. | Parker Ltd. |
|---|---|---|
| **Non-current assets:** | | |
| Property, plant and equipment | 400 | 600 |
| Investment | 300 | 200 |
| **Current assets:** | | |
| Inventories | 300 | 100 |
| Financial assets | | |
| Trade receivables | 400 | 200 |
| Cash and cash equivalents | 150 | 200 |
| Others | 300 | 300 |
| Total | 1,850 | 1,600 |
| **Equity and Liabilities** | | |
| **Equity** | | |
| Share capital - Equity shares of Rs. 100 each for Parker Ltd. &Rs. 10each for David Limited | 500 | 400 |
| Other Equity | 700 | 275 |
| **Non-current liabilities:** | | |
| Long term borrowings | 200 | 300 |
| Long term provisions | 100 | 80 |
| Deferred tax | 20 | 55 |
| **Current liabilities:** | | |
| Short term borrowings | 130 | 170 |
| Trade payables | 200 | 320 |
| Total | 1,850 | 1,600 |

Other Information:

(i) David Ltd. acquired 70% shares of Parker Ltd. on 1st April, 20X1·by issuing its own shares in the ratio of 1 share of David Ltd. for every 2 shares of Parker Ltd. The fair value of the shares of David Ltd. was Rs. 50 per share.

(ii) The fair value exercise resulted in the following :

(1) Fair value of property, plant and equipment (PPE) on 1st April, 20X1 was Rs. 450 lakh.

(2) David Ltd. agreed to pay an additional payment as consideration that is higher of Rs. 30 lakh and 25% of any excess profits in the first year after acquisition, over its profits in the preceding 12 months made by Parker Ltd. This additional amount will be due after 3 years. Parker Ltd. has earned Rs. 20 lakh profit in the preceding year and expects to earn another Rs. 10 lakh.

(3) In addition to above, David Ltd. also has agreed to pay one of the founder shareholder-Director a payment of Rs. 25 lakh provided he stays with the Company for two years after the acquisition.

(4) Parker Ltd. had certain equity settled share-based payment award (original award) which got replaced by the new awards issued by David Ltd. As per the original term, the vesting period was 4 years and as of the acquisition date the employees of Parker Ltd. have already served 2 years of service. As per the replaced awards, the vesting period has been reduced to one year (one year from the acquisition date). The fair value of the award on the acquisition date was as follows:

Original award - Rs. 6 lakh

Replacement award - Rs. 9 lakh

(5) Parker Ltd. had a lawsuit pending with a customer who had made a claim of Rs. 35 lakh. Management reliably estimated the fair value of the liability to be Rs. 10 lakh.

(6) The applicable tax rate for both entities is 40%.

You are required to prepare opening consolidated balance sheet of David Ltd. as on 1st April, 20X1 along with workings. Assume discount rate of 8%. **(16 Marks)**

(b) A farmer owned a dairy herd of three years old cattle as at 1st April, 20X1 with a fair value of Rs. 13,750 and the number of cattle in the herd was 250.

The fair value of three year cattle as at 31st March, 20X2 was Rs. 60 per cattle. The fair value of four year cattle as at 31st March, 20X2 is Rs. 75 per cattle.

Calculate the measurement of group of cattle as at 31st March, 20X2 stating price and physical change separately. **(4 Marks)**

4. (a) CAB Limited is in the process of preparation of the consolidated financial statements of the group for the year ending 31st March, 20X3 and the extract of the same is as follows:

| Particulars | Attributable to CAB Limited | Non-controlling interest | Total (Rs. in '000) |
|---|---|---|---|
| Profit for the year | 39,000 | 3,000 | 42,000 |
| Other Comprehensive Income | 5,000 | Nil | 5,000 |
| Total Comprehensive Income | 44,000 | 3,000 | 47,000 |

The long-term finance of the company comprises of the following:

(i) 20,00,00,000 equity shares at the beginning of the year and the company has issued 5,00,00,000 shares on 1st July, 20X2 at full market value.

(ii) 8,00,00,000 irredeemable preference shares. These shares were in issue for the whole of the year ended 31st March, 20X3. The dividend on these preference shares is discretionary.

(iii) Rs. 18 crores of 6% convertible debentures issued on 1st April, 20X1 and repayable on 31st March, 20X5 at par. Interest is payable annually. As an alternative to repayment at par, the holder on maturity can elect to exchange their convertible debentures for 10 crores ordinary shares in the company. On 1st April, 20X1, the prevailing market interest rate for four-year convertible debentures which had no right of conversion was 8%. Using an annual discount rate of 8%, the present value of Rs. 1 payable in four years is 0.74 and the cumulative present value of Rs. 1 payable at the end of years one to four is 3.31.

In the year ended 31st March, 20X3, CAB Limited declared an ordinary dividend of 0.10 paise per share and a dividend of 0.05 paise per share on the irredeemable preference shares.

Compute the following:

- the finance cost of convertible debentures and its closing balance as on 31st March, 20X3 to be presented in the consolidated financial statements.
- the basic and diluted earnings per share for the year ended 31st March, 20X3.

Assume that income tax is applicable to CAB Limited and its subsidiaries at 25%. **(12 Marks)**

(b) Mr. Niranjan is working for Infotech Ltd. Consider the following particulars:

| | Year 20X0-20X1 | Year 20X1-20X2 |
|---|---|---|
| Annual salary | Rs. 30,00,000 | Rs. 30,00,000 |
| No. of working days during the year | 300 days | 300 days |
| Leave allowed | 10 days | 10 days |
| Leave taken | 7 days | 13 days |
| Leave unutilized carried forward to next year | 3 days | NIL |

Based on past experience, Infotech Ltd. assumes that Mr. Niranjan will avail the unutilized leaves of 3 days of 20X0-20X1 in 20X1-20X2.

Infotech Ltd. contends that it will record Rs. 30,00,000 as employee benefits expense in each of the years 20X0-20X1 and 20X1-20X2, stating that the leaves will, in any case, be utilized by 20X1-20X2.

Comment on the accounting treatment proposed to be followed by Infotech Ltd. Also pass journal entries for both the years. **(8 Marks)**

5. (a) ABC Limited manufactures automobile parts. ABC Limited has shown a net profit of Rs. 20,00,000 for the third quarter of 20X1.

Following adjustments are made while computing the net profit:

(i) Bad debts of Rs. 1,00,000 incurred during the quarter. 50% of the bad debts have been deferred to the next quarter.

(ii) Additional depreciation of Rs. 4,50,000 resulting from the change in the method of depreciation.

(iii) Exceptional loss of Rs. 28,000 incurred during the third quarter. 50% of exceptional loss have been deferred to next quarter.

(iv) Rs. 5,00,000 expenditure on account of administrative expenses pertaining to the third quarter is deferred on the argument that the fourth quarter will have more sales; therefore fourth quarter should be debited by higher expenditure. The expenditures are uniform throughout all quarters.

Analyze and ascertain the correct net profit to be shown in the Interim Financial Report of third quarter to be presented to the Board of Directors. **(5 Marks)**

(b) Buildings Limited with a financial year end of 31st March, entered into a contract with its customer, Radar Limited, to build a manufacturing facility. Buildings Limited determines that the contract contains one performance obligation satisfied over time. Construction is scheduled to be completed by the end of the 36th month for an agreed upon price of Rs. 25 crores. Buildings Limited has the opportunity to earn a performance bonus for early completion as follows:

- 15% bonus of the contract price if completed by the 30th months (25% likelihood).
- 10% bonus of the contract price if completed by the 32nd months (40% likelihood).
- 5% bonus of the contract price if completed by the 34th months (15% likelihood).

In addition to the potential performance bonus for early completion, Buildings Limited is entitled to a quality bonus of Rs. 2 crores if a health and safety inspector assigns the facility a gold star rating as defined by Radar Limited in terms of the contract. Buildings Limited concludes that it is 60% likely that it will receive the quality bonus.

Analyze and determine the amount of variable consideration Building Limited should recognize in its contract with Radar Company Limited to build a manufacturing facility. **(5 Marks)**

(c) Entity AB Ltd. enters into a three-year service contract with a customer CD Ltd. for Rs. 4,50,000 (Rs.1,50,000 per year). The standalone selling price for one year of service at inception of the contract is Rs.1,50,000 per year. AB Ltd. accounts for the contract as a series of distinct services.

At the beginning of the third year, the parties agree to modify the contract as follows:

(i) the fee for the third year is reduced to Rs.1,20,000; and

(ii) CD Ltd. agrees to extend the contract for another three years for Rs.3,00,000 (Rs.1,00,000 per year).

The standalone selling price for one year of service at the time of modification is Rs. 1,20,000. How should AB Ltd. account for the modification? Analyze. **(5 Marks)**

(d) An entity charged off certain expenses as finance costs in its financial statements for the year ended 31st March 20X1. While preparing annual financial statements for the year ended 31st March 20X2, management 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 20X1). Would this reclassification of expenses from finance costs to other expenses in the comparative amounts be considered to be correction of an error under Ind AS 8? Would the entity need to present a third balance sheet? **(5 Marks)**

6. (a) New Age Technology Limited has entered into following Share Based payment transactions:

(i) On 1st April, 20X1, New Age Technology Limited decided to grant share options to its employees. The scheme was approved by the employees on 30th June, 20X1. New Age Technology Limited determined the fair value of the share options to be the value of the equity shares on 1st April, 20X1.

(ii) On 1st April, 20X1, New Age Technology Limited entered into a contract to purchase IT equipment from Bombay Software Limited and agreed that the contract will be settled by issuing equity instruments of New Age Technology Limited. New Age Technology Limited received the IT equipment on 30th July, 20X1. The share-based payment transaction was measured based on the fair value of 'the equity instruments as on 1st April, 20X1.

(iii) On 1st April, 20X1, New Age Technology Limited decided to grant the share options to its employees. The scheme was approved by the employees on 30th June, 20X1. The issue of the share options was however subject to the same being approved by the shareholders in a general meeting. The scheme was approved in the general meeting held on 30th September, 20X1. The fair value of the equity instruments for measuring the share-based payment transaction was taken on 30th September, 20X1.

Identify the grant date and measurement date in all the 3 cases of Share based payment transactions entered into by New Age Technology Limited, supported by appropriate rationale for the determination? **(8 Marks)**

(b) Entity A has undertaken various transactions in the financial year ended 31st March, 20X1. Identify and present the transactions in the financial statements as per Ind AS 1. Rs.

| | |
|---|---|
| Remeasurement of defined benefit plans | 2,57,000 |
| Current service cost | 1,75,000 |
| Changes in revaluation surplus | 1,25,000 |
| Gains and losses arising from translating the monetary assets in foreign currency | 75,000 |
| Gains and losses arising from translating the financial statements of a foreign operation | 65,000 |
| Gains and losses from investments in equity instruments designated at fair value through other comprehensive income | 1,00,000 |
| Income tax expense | 35,000 |
| Share based payments cost | 3,35,000 |

**(4 Marks)**

(c) A Ltd. (the 'Company') makes a borrowing for Rs. 10 lacs from RBC Bank, with bullet repayment of Rs. 10 lacs and an annual interest rate of 12% per annum. Now, Company defaults at the end of 5th year and consequently, a rescheduling of the payment schedule is made beginning 6th year onwards. The Company is required to pay Rs. 1,300,000 at the end of 6th year for one time settlement, in lieu of defaults in payments made earlier.

(a) Does the above instrument meet definition of financial liability? Please explain.

(b) Analyse the differential amount to be exchanged for one-time settlement **(4 Marks)**

(d) State the major changes in Ind AS 2 vis-a-vis AS 2 in respect of the following namely:

(i) Machinery Spares

(ii) Subsequent assessment of Net Realisable value

(iii) Cost Formulae **(4 Marks)**

OR

A construction services company enters into a contract with a customer to build a water purification plant. The company is responsible for all aspects of the plant including overall project management, engineering and design services, site preparation, physical construction of the plant, procurement of pumps and equipment for measuring and testing flow volumes and water quality, and the integration of all components.

Determine whether the company has a single or multiple performance obligations under the contract? **(4 Marks)**