

MOCK TEST PAPER 2
FINAL COURSE: GROUP – I
PAPER – 1: FINANCIAL REPORTING
ANSWERS

1. (a) Balance Sheet of Master Creator Private Limited as at 31st March, 20X2

Particulars	Working/Note reference	(₹)
ASSETS		
Non-current assets		
Property, plant and equipment	1	49,87,750
Capital work-in-progress	2	20,01,600
Investment Property	3	15,48,150
Financial assets		
Other financial assets (Security deposits)		4,62,500
Other non-current assets (capital advances)	4	17,33,480
Current assets		
Inventories		5,98,050
Financial assets		
Investments (55,000 + 5,000)	5	60,000
Trade receivables	6	7,25,000
Cash and cash equivalents	7	1,16,950
Other financial assets	8	1,27,370
Other current assets (Prepaid expenses)	8	90,000
TOTAL ASSETS		1,24,50,850
EQUITY AND LIABILITIES		
Equity		
Equity share capital	A	10,00,000
Other equity	B	28,44,606
Non-current liabilities		
Financial liabilities		
8% Convertible loan	11	60,60,544
Long term provisions		5,24,436
Deferred tax liability	12	2,20,700
Current liabilities		
Financial liabilities		
Trade payables	13	6,69,180
Other financial liabilities	14	1,19,299
Other current liabilities (TDS payable)	15	81,265
Current tax liabilities		9,30,820
TOTAL EQUITY AND LIABILITIES		1,24,50,850

Statement of changes in equity
For the year ended 31st March, 20X2

A. Equity Share Capital

	Balance (₹)
As at 31 st March, 20X1	10,00,000
Changes in equity share capital during the year	<u>-</u>
As at 31 st March, 20X2	<u>10,00,000</u>

B. Other Equity

	Retained Earnings (₹)	Equity component of Compound Financial Instrument (₹)	Total (₹)
As at 31 st March, 20X1	21,25,975	-	21,25,975
Total comprehensive income for the year (25,00,150 + 5,000 - 85,504 - 21,25,975)	2,93,671	-	2,93,671
Issue of compound financial instrument during the year	<u>-</u>	<u>4,24,960</u>	<u>4,24,960</u>
As at 31st March, 20X2	<u>24,19,646</u>	<u>4,24,960</u>	<u>28,44,606</u>

Disclosure forming part of Financial Statements:

Proposed dividend on equity shares is subject to the approval of the shareholders of the company at the annual general meeting and not recognized as liability as at the Balance Sheet date. (Note 9)

Notes/ Workings: (for adjustments/ explanations)

- Property, plant and equipment are tangible items that: (a) are held for use in the production or supply of goods or services, for rental to others, or for administrative purposes; and (b) are expected to be used during more than one period. Therefore, the items of PPE are Buildings (₹ 37,50,250) and Vehicles (₹ 12,37,500), since those assets are held for administrative purposes.
- Property, plant and equipment which are not ready for intended use as on the date of Balance Sheet are disclosed as "Capital work-in-progress". It would be classified from PPE to Capital work-in-progress.
- Investment property is property (land or a building—or part of a building—or both) held (by the owner or by the lessee as a right-of-use asset) to earn rentals or for capital appreciation or both, rather than for:
 - use in the production or supply of goods or services or for administrative purposes; or
 - sale in the ordinary course of business.

Therefore, Land held for capital appreciation should be classified as Investment property rather than PPE.
- Assets for which the future economic benefit is the receipt of goods or services, rather than the right to receive cash or another financial asset, are not financial assets.

5. Current investments here are held for the purpose of trading. Hence, it is a financial asset classified as FVTPL. Any gain in its fair value will be recognised through profit or loss. Hence, ₹ 5,000 (60,000 – 55,000) increase in fair value of financial asset will be recognised in profit and loss.
6. A contractual right to receive cash or another financial asset from another entity is a financial asset. Trade receivables is a financial asset in this case and hence should be reclassified.
7. Cash is a financial asset. Hence it should be reclassified.
8. Other current financial assets:

Particulars	Amount (₹)
Interest accrued on bank deposits	57,720
Royalty receivable from dealers	69,650
Total	1,27,370

Prepaid expenses does not result into receipt of any cash or financial asset. However, it results into future goods or services. Hence, it is not a financial asset.

9. As per Ind AS 10, 'Events after the Reporting Period', If dividends are declared after the reporting period but before the financial statements are approved for issue, the dividends are not recognized as a liability at the end of the reporting period because no obligation exists at that time. Such dividends are disclosed in the notes in accordance with Ind AS 1, Presentation of Financial Statements.
10. 'Other Equity' cannot be shown under 'Non-current liabilities'. Accordingly, it is reclassified under 'Equity'.
11. There are both 'equity' and 'debt' features in the instrument. An obligation to pay cash i.e. interest at 8% per annum and a redemption amount will be treated as 'financial liability' while option to convert the loan into equity shares is the equity element in the instrument. Therefore, convertible loan is a compound financial instrument.

Calculation of debt and equity component and amount to be recognised in the books:

S. No	Year	Interest amount @ 8%	Discounting factor @ 10%	Amount
Year 1	20X2	5,12,000	0.91	4,65,920
Year 2	20X3	5,12,000	0.83	4,24,960
Year 3	20X4	5,12,000	0.75	3,84,000
Year 4	20X5	69,12,000	0.68	<u>47,00,160</u>
Amount to be recognised as a liability				59,75,040
Initial proceeds				<u>(64,00,000)</u>
Amount to be recognised as equity				<u>4,24,960</u>

* In year 4, the loan note will be redeemed; therefore, the cash outflow would be ₹ 69,12,000 (₹ 64,00,000 + ₹ 5,12,000).

Presentation in the Financial Statements:**In Statement of Profit and Loss for the year ended on 31 March 20X2**

Finance cost to be recognised in the Statement of Profit and Loss (59,75,040 x 10%)	₹ 5,97,504
Less: Already charged to the Statement of Profit and Loss	<u>(₹ 5,12,000)</u>
Additional finance charge required to be recognised in the Statement of Profit and Loss	<u>₹ 85,504</u>

In Balance Sheet as at 31 March 20X2

Equity and Liabilities	
Equity	
Other Equity (8% convertible loan)	4,24,960
Non-current liability	
Financial liability [8% convertible loan – [(59,75,040+ 5,97,504– 5,12,000)]]	60,60,544

12. Since entity has the intention to set off deferred tax asset against deferred tax liability and the entity has a legally enforceable right to set off taxes, hence their balance on net basis should be shown as:

Particulars	Amount (₹)
Deferred tax liability	4,74,850
Deferred tax asset	<u>(2,54,150)</u>
Deferred tax liability (net)	<u>2,20,700</u>

13. A liability that is a contractual obligation to deliver cash or another financial asset to another entity is a financial liability. Trade payables is a financial liability in this case.
14. 'Other current financial liabilities':

Particulars	Amount (₹)
Wages payable	21,890
Salary payable	61,845
Interest accrued on trade payables	35,564
Total	<u>1,19,299</u>

15. Liabilities for which there is no contractual obligation to deliver cash or other financial asset to another entity, are not financial liabilities. Hence, TDS payable should be reclassified from 'Other current financial liabilities' to 'Other current liabilities' since it is not a contractual obligation.

(b) Following entries would be passed in the books of A Ltd.:

1) Initial entry to record investment done in associate

Investment in B Ltd. A/c	Dr.	1,00,000	
To Bank A/c			1,00,000

2) Recording of share in the profit of the associate

Investment in B Ltd. A/c	Dr.	2,500	
To Share in profit of investee (P&L)			2,500
[A Ltd. share in profit would be ₹ 2,500 (₹ 10,000 x 25%)]			

3) Recording of share in the other comprehensive income (OCI) of the associate

Investment in B Ltd. A/c	Dr.	500	
To Share in OCI of investee (OCI)			500
[A Ltd. share in OCI would be ₹ 500 (₹ 2,000 x 25%)]			

4) Recording of dividend distributed by associate

Dividend Receivable A/c	Dr.	1,000	
To Investment in B Ltd. A/c			1,000
[A Ltd. share in dividend would be ₹ 1,000 (₹ 4,000 x 25%)]			

2. (a) Para 36 of Ind AS 7 inter alia states that when it is practicable to identify the tax cash flow with an individual transaction that gives rise to cash flows that are classified as investing or financing activities the tax cash flow is classified as an investing or financing activity as appropriate. When tax cash flows are allocated over more than one class of activity, the total amount of taxes paid is disclosed.

Accordingly, the transactions are analysed as follows:

Particulars	Amount (in crore)	Activity
Sale Consideration	100	Investing Activity
Capital Gain Tax	(20)	Investing Activity
Business profits	30	Operating Activity
Tax on Business profits	(3)	Operating Activity
Dividend Payment	(20)	Financing Activity
Dividend Distribution Tax	(2)	Financing Activity
Income Tax Refund	<u>1.5</u>	Operating Activity
Total Cash flow	<u>86.5</u>	

Activity wise	Amount (in crore)
Operating Activity	28.5
Investing Activity	80
Financing Activity	<u>(22)</u>
Total	<u>86.5</u>

- (b) The value of closing inventory in the financial statements:

Item of inventory	Cost	NRV (Estimated Sales price- Selling costs)	Measurement base (lower of cost or NRV)	Value
A1	8,000	(7,800 – 500) 7,300	NRV	7,300
A2	14,000	(18,000 – 200) 17,800	Cost	14,000
B1	16,000	(17,000 – 200) 16,800	Cost	16,000
C1	6,000	(7,500 – 150) 7,350	Cost	<u>6,000</u>
Value of Inventory				<u>43,300</u>

(c) (A) Calculation of employee compensation expense

	Year 1	Year 2	
Expected employees to remain in the employment during the vesting period	180	190	
Fair value of option	18	18	
Number of options	<u>1,000</u>	<u>1,000</u>	
Total	<u>32,40,000</u>	<u>34,20,000</u>	
Expense weightage	1/3	2/3	Balance 2/3 rd in full, as it is cancelled
Expense for the year	10,80,000	23,40,000	Remaining amount since cancelled

(B) Cancellation compensation to be charged in the year 2

Cancellation compensation			
Number of employees (A)	190		
Amount agreed to pay (B)	13.50		
Number of options/ employee (C)	1,000		
Compensation amount (A x B x C)			25,65,000
Less: Amount to be deducted from Equity			
Number of employees (D)	190		
Fair value of option (at the date of cancellation) (E)	12		
Number of options / employee (F)	1,000		
Amount to be deducted from Equity (D x E x F)			<u>(22,80,000)</u>
Balance transferred to Profit and Loss			<u>2,85,000</u>

- (d) The transaction price is ₹ 90 per container based on entity J's estimate of total sales volume for the year, since the estimated cumulative sales volume of 2.8 million containers would result in a price per container of ₹ 90. Entity J concludes that based on a transaction price of ₹ 90 per container, it is highly probable that a significant reversal in the amount of cumulative revenue recognised will not occur when the uncertainty is resolved. Revenue is therefore recognised at a selling price of ₹ 90 per container as each container is sold. Entity J will recognise a liability for cash received in excess of the transaction price for the first 1 million containers sold at ₹ 100 per container (that is, ₹ 10 per container) until the cumulative sales volume is reached for the next pricing tier and the price is retroactively reduced.

For the quarter ended 31st March, 20X8, entity J recognizes revenue of ₹ 63 million (700,000 containers x ₹ 90) and a liability of ₹ 7 million [700,000 containers x (₹ 100 - ₹ 90)].

Entity J will update its estimate of the total sales volume at each reporting date until the uncertainty is resolved.

3. (a) On initial measurement, Entity X will measure the lease liability and ROU asset as under:

Year	Lease Payments (USD)	Present Value factor @ 5%	Present Value of Lease Payment	Conversion rate (spot rate)	INR value
1	10,000	0.952	9,520	68	6,47,360

2	10,000	0.907	9,070	68	6,16,760
3	10,000	0.864	8,640	68	5,87,520
4	10,000	0.823	8,230	68	5,59,640
5	10,000	0.784	<u>7,840</u>	68	<u>5,33,120</u>
Total			<u>43,300</u>		<u>29,44,400</u>

As per Ind AS 21 *The Effects of Changes in Foreign Exchange Rates*, monetary assets and liabilities are restated at each reporting date at the closing rate and the difference due to foreign exchange movement is recognised in profit and loss whereas non-monetary assets and liabilities carried measured in terms of historical cost in foreign currency are not restated.

Accordingly, the ROU asset in the given case being a non-monetary asset measured in terms of historical cost in foreign currency will not be restated but the lease liability being a monetary liability will be restated at each reporting date with the resultant difference being taken to profit and loss.

At the end of Year 1, the lease liability will be measured in terms of USD as under:

Lease Liability:

Year	Initial Value (USD) (a)	Lease Payment (b)	Interest @ 5% (c) = (a x 5%)	Closing Value (USD) (d = a + c - b)
1	43,300	10,000	2,165	35,465

Interest at the rate of 5% will be accounted for in profit and loss at average rate of ₹ 69 (i.e., USD 2,165 x 69) = ₹ 1,49,385.

Particulars	Dr. (₹)	Cr. (₹)
Interest Expense Dr. To Lease liability	1,49,385	1,49,385

Lease payment would be accounted for at the reporting date exchange rate, i.e. ₹ 70 at the end of year 1

Particulars	Dr. (₹)	Cr. (₹)
Lease liability Dr. To Cash	7,00,000	7,00,000

As per the guidance above under Ind AS 21, the lease liability will be restated using the reporting date exchange rate i.e., ₹ 70 at the end of Year 1. Accordingly, the lease liability will be measured at ₹ 24,82,550 (35,465 x ₹ 70) with the corresponding impact due to exchange rate movement of ₹ 88,765 (24,82,550 – (29,44,400 + 1,49,385 – 700,000) taken to profit and loss.

At the end of year 1, the ROU asset will be measured as under:

Year	Opening Balance (₹)	Depreciation (₹)	Closing Balance (₹)
1	29,44,400	5,88,880	23,55,520

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

a. Computation of Liability & Equity Component

Date	Particulars	Cash Flow	Discount Factor	Net present Value
01-Apr-20X1		0	1	0.00
31-Mar-20X2	Dividend	150,000	0.870	130,500
31-Mar-20X3	Dividend	150,000	0.756	113,400
31-Mar-20X4	Dividend	150,000	0.658	98,700
31-Mar-20X5	Dividend	150,000	0.572	85,800
31-Mar-20X6	Dividend	150,000	0.497	<u>74,550</u>
Total Liability Component				502,950
Total Proceeds				<u>1,500,000</u>
Total Equity Component (Bal fig)				<u>997,050</u>

b. Allocation of transaction costs

Particulars	Amount	Allocation	Net Amount
Liability Component	502,950	10,059	492,891
Equity Component	<u>997,050</u>	<u>19,941</u>	<u>977,109</u>
Total Proceeds	<u>1,500,000</u>	<u>30,000</u>	<u>1,470,000</u>

c. Accounting for liability at amortised cost:

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

	Opening Financial Liability A	Interest B	Cash Flow C	Closing Financial Liability A+B-C
01-Apr-20X1	492,891	-	-	4,92,891
31-Mar-20X2	492,891	78,173	150,000	4,21,064
31-Mar-20X3	421,064	66,781	150,000	3,37,845
31-Mar-20X4	337,845	53,582	150,000	2,41,427
31-Mar-20X5	241,427	38,290	150,000	1,29,717
31-Mar-20X6	129,717	20,283	150,000	-

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

Date	Particulars	Debit	Credit
01-Apr-20X1	Bank A/c Dr. To Preference Shares A/c To Equity Component of Preference shares A/c (Being compulsorily convertible preference shares issued. The same are divided into equity component and liability component as per the calculation)	1,470,000	492,891 977,109

31-Mar-20X2	Preference shares A/c Dr. To Bank A/c (Being Dividend at the coupon rate of 10% paid to the shareholders)	150,000	150,000
31-Mar-20X2	Finance cost A/c Dr. To Preference Shares A/c (Being interest as per EIR method recorded)	78,173	78,173
31-Mar-20X3	Preference shares A/c Dr. To Bank A/c (Being Dividend at the coupon rate of 10% paid to the shareholders)	150,000	150,000
31-Mar-20X3	Finance cost A/c Dr. To Preference Shares A/c (Being interest as per EIR method recorded)	66,781	66,781
31-Mar-20X4	Preference shares A/c Dr. To Bank A/c (Being Dividend at the coupon rate of 10% paid to the shareholders)	150,000	150,000
31-Mar-20X4	Finance cost A/c Dr. To Preference Shares A/c (Being interest as per EIR method recorded)	53,582	53,582
31-Mar-20X5	Preference shares A/c Dr. To Bank A/c (Being Dividend at the coupon rate of 10% paid to the shareholders)	150,000	150,000
31-Mar-20X5	Finance cost A/c Dr. To Preference Shares A/c (Being interest as per EIR method recorded)	38,290	38,290
31-Mar-20X6	Preference shares A/c Dr. To Bank A/c (Being Dividend at the coupon rate of 10% paid to the shareholders)	150,000	150,000
31-Mar-20X6	Finance cost A/c Dr. To Preference Shares A/c (Being interest as per EIR method recorded)	20,283	20,283
31-Mar-20X6	Equity Component of Preference shares A/c Dr. To Equity Share Capital A/c To Securities Premium A/c (Being Preference shares converted in equity shares and remaining equity component is recognised as securities premium)	977,109	50,000 927,109

4. (a)

	20X3	20X2
Trading results	₹	₹
A. Profit before interest, fair value movements and tax	17,90,000	16,50,000
B. Interest on 8% convertible loan stock (20X2: $9/12 \times ₹ 2,00,000$)	(2,00,000)	(1,50,000)
C. Change in fair value of embedded option	<u>(5,300)</u>	<u>(5,000)</u>
Profit before tax	15,84,700	14,95,000
Taxation @ 33% on (A-B)	<u>(5,24,700)</u>	<u>(4,95,000)</u>
Profit after tax	<u>10,60,000</u>	<u>10,00,000</u>
Calculation of basic EPS		
Number of equity shares outstanding	20,00,000	20,00,000
Earnings	10,60,000	10,00,000
Basic EPS	53 paise	50 paise

Calculation of diluted EPS

Test whether convertibles are dilutive:

The saving in after-tax earnings, resulting from the conversion of ₹ 100 nominal of loan stock, amounts to $(₹ 100 \times 8\% \times 67\%) + (₹ 5,300 / 25,000) = ₹ 5.36 + ₹ 0.21 = ₹ 5.57$.

There will then be 135 extra shares in issue.

Therefore, the incremental EPS is 4 paise (ie. $₹ 5.57 / 135$). As this incremental EPS is less than the basic EPS at the continuing level, it will have the effect of reducing the basic EPS of 53 paise. Hence the convertibles are dilutive.

	20X3	20X2
Adjusted earnings	₹	₹
Profit for basic EPS	10,60,000	10,00,000
Add: Interest and other charges on earnings saved as a result of the conversion	(2,00,000 + 5,300) 2,05,300	(1,50,000 + 5,000) 1,55,000
Less: Tax relief on interest portion	<u>(66,000)</u>	<u>(49,500)</u>
Adjusted earnings for equity	<u>11,99,300</u>	<u>11,05,500</u>

Adjusted number of shares

From the conversion terms, it is clear that the maximum number of shares issuable on conversion of ₹ 25,00,000 loan stock after the end of the financial year would be at the rate of 135 shares per ₹ 100 nominal (that is, 33,75,000 shares).

	20X3	20X2
Number of equity shares for basic EPS	20,00,000	20,00,000
Maximum conversion at date of issue ($33,75,000 \times 9/12$)	-	25,31,250
Maximum conversion after balance sheet date	<u>33,75,000</u>	<u>-</u>
Adjusted shares	<u>53,75,000</u>	<u>45,31,250</u>
Adjusted earnings for equity	11,99,300	11,05,500
Diluted EPS (approx.)	22 paise	24 paise

- (b) (i) In order to fit into the definition of a joint arrangement, the parties to the joint arrangement should have joint control over the arrangement. In the given case, decisions relating to relevant activities, ie, marketing and distribution, are solely controlled by X Ltd and such decisions do not require the consent of Y Ltd. Hence, the joint control test is not satisfied in this arrangement and the arrangement does not fit into the definition of a joint arrangement in accordance with the Standard.
- (ii) Where X Ltd and Y Ltd both jointly control all the relevant activities of the arrangement and since no separate entity is formed for the arrangement, the joint arrangement is in the nature of a *joint operation*.
- (iii) Where under a joint arrangement, a separate vehicle is formed to give effect to the joint arrangement, then the joint arrangement can either be a joint operation or a joint venture.

Hence in the given case, if:

- (a) The contractual terms of the joint arrangement, give both X Ltd and Y Ltd rights to the assets and obligations for the liabilities relating to the arrangement, and the rights to the corresponding revenues and obligations for the corresponding expenses, then the joint arrangement will be in the nature of a joint operation.
- (b) The contractual terms of the joint arrangement, give both X Ltd and Y Ltd. rights to the net assets of the arrangement, then the joint arrangement will be in the nature of a joint venture.
- (iv) Where the rights to assets and liabilities to obligations are not clear from the contractual arrangement, then other facts and circumstances also need to be considered to determine whether the joint arrangement is a joint operation or a joint venture.

When the provision of the activities of the joint venture is primarily to produce output and the output is available / distributed only to the parties to the joint arrangement in some pre-determined ratio, then this indicates that the parties have substantially all the economic benefits of the assets of the arrangement. The only source of cash flows to the joint arrangement is receipts from parties through their purchases of the output and the parties also have a liability to fund the settlement of liabilities of the separate entity. Such an arrangement indicates that the joint arrangement is in the nature of a joint operation.

In the given case, the output of the joint arrangement is exclusively used by X Ltd. and Y Ltd. and the joint arrangement is not allowed to sell the output to outside parties. Hence, the joint arrangement between X Ltd. and Y Ltd. is in the nature of a joint operation.

- (v) It makes no difference whether the output of the joint arrangement is exclusively for use by the parties to the joint arrangement or the parties to the arrangement sold their share of the output to third parties.

Hence, even if X Ltd. and Y Ltd. sold their respective share of output to third parties, the fact still remains that the joint arrangement cannot sell output directly to third parties. Hence, the joint arrangement will still be deemed to be in the nature of a *joint operation*.

- (vi) Where the terms of the contractual arrangement enable the separate entity to sell the output to third parties, this would result in the separate entity assuming demand, inventory and credit risks. Such facts and circumstances would indicate that the arrangement is a joint venture.

For a joint arrangement to be either a *joint operation* or *joint venture*, it depends on whether the parties to the joint arrangement have rights to the assets and obligations for liabilities (will be a joint operation) OR whether the parties to the joint arrangement have rights to the net assets of the arrangement (will be joint venture).

(c) An entity has eight segments and the relevant information is as follows:

Criteria 1: Segment revenue is 10% or more of total external + intersegment sales

Segments	A	B	C	D	E	F	G	H	Total
Total sales	100	315	45	15	15	50	25	35	600
% to total sales	16.7	52.5	7.5	2.5	2.5	8.3	4.2	5.8	
Reportable segments	A	B	-	-	-	-	-	-	

Criteria 2: 10% or more of segment result

Consider segment profit and loss separately in absolute terms

Segments	A	B	C	D	E	F	G	H	Total
Profit	5	-	15	-	8	-	5	7	40
Segments loss	-	90	-	5	-	5	-	-	100

Since segment loss is greater, we select 100 as evaluating the segment percentage

Segments	A	B	C	D	E	F	G	H	Total
% to segment loss	5	90	15	5	8	5	5	7	
Reportable segments	-	B	C	-	-	-	-	-	

Criteria 3: 10% or more of segment assets

Segments	A	B	C	D	E	F	G	H	Total
Assets	15	47	5	11	3	5	5	9	100
%	15	47	5	11	3	5	5	9	100
Reportable segments	A	B	-	D	-	-	-	-	

Based on the above 3 criteria, the Reportable Segments are A, B, C & D

However, 75% test for external sales should also be checked.

Reportable Segments	A	B	C	D	TOTAL
External sales	0	255	15	10	280
Total entity's sales (external)					405
% of reportable segments external sales to entity's sales					69.14%
Required percentage					75%

Hence, in the above scenario, additional operating segments need to be identified as reportable segments, till the 75% test is satisfied, even if those segments do not satisfy the quantitative threshold limits.

5. (a) Calculation of the value in use of the machine owned by E Ltd. includes the projected cash inflow (i.e. sales income) from the continued use of the machine and projected cash outflows that are necessarily incurred to generate those cash inflows (i.e cost of goods sold). Additionally, projected cash inflows include ₹ 80,000 from the disposal of the asset in March, 20X8. Cash outflows include routing capital expenditures of ₹ 50,000 in 20X5-20X6.

As per Ind AS 36, estimates of future cash flows shall not include:

- Cash inflows from receivables
- Cash outflows from payables
- Cash inflows or outflows expected to arise from future restructuring to which an entity is not

yet committed

- Cash inflows or outflows expected to arise from improving or enhancing the asset's performance
- Cash inflows or outflows from financing activities
- Income tax receipts or payments.

Hence in this case, cash flows do not include financing interest (i.e. 10%), tax (i.e. 30%) and capital expenditures to which E Ltd. has not yet committed (i.e. ₹ 1,00,000). They also do not include any savings in cash outflows from these capital expenditures, as required by Ind AS 36.

The cash flows (inflows and outflows) are presented below in nominal terms. They include an increase of 3% per annum to the forecast price per unit (B), in line with forecast inflation. The cash flows are discounted by applying a discount rate (8%) that is also adjusted for inflation.

Note: Figures are calculated on full scale and then rounded off to the nearest absolute value.

Year ended	20X3-20X4	20X4-20X5	20X5-20X6	20X6-20X7	20X7-20X8	Value in use
Quantity (A)	10,000	10,500	11,025	11,576	12,155	
Price per unit (B)	₹ 200	₹ 206	₹ 212	₹ 219	₹ 225	
Estimated cash inflows (C=A x B)	₹ 20,00,000	₹ 21,63,000	₹ 23,37,300	₹ 25,35,144	₹ 27,34,875	
Misc. cash inflow disposal proceeds (D)					₹ 80 000	
Total estimated cash inflows (E=C+D)	₹ 20,00,000	₹ 21,63,000	₹ 23,37,300	₹ 25,35,144	₹ 28,14,875	
Cost per unit (F)	₹ 160	₹ 162	₹ 165	₹ 168	₹ 171	
Estimated cash outflows (G = A x F)	(₹16,00,000)	(₹17,01,000)	(₹18,19,125)	(₹19,44,768)	(₹20,78,505)	
Misc. cash outflow: maintenance costs (H)			(₹ 50,000)			
Total estimated cash outflows (I=G+H)	(₹16,00,000)	(₹17,01,000)	(₹18,69,125)	(₹19,44,768)	(₹20,78,505)	
Net cash flows (J=E-I)	₹ 4,00,000	₹ 4,62,000	₹ 4,68,175	₹ 5,90,376	₹ 7,36,370	
Discount factor 8% (K)	0.9259	0.8573	0.7938	0.7350	0.6806	
Discounted future cash flows (L=J x K)	₹ 3,70,360	₹ 3,96,073	₹ 3,71,637	₹ 4,33,926	₹ 5,01,173	₹20,73,169

(b) For the year 20X1-20X2

S Limited accounts for the promised bundle of goods and services as a single performance obligation satisfied over time in accordance with Ind AS 115. At the inception of the contract, S Limited expects the following:

Transaction price	– ₹ 20,00,000
Expected costs	– ₹ 11,00,000
Expected profit (45%)	– ₹ 9,00,000

At contract inception, S Limited excludes the ₹ 2,50,000 bonus from the transaction price because it cannot conclude that it is highly probable that a significant reversal in the amount of cumulative revenue recognised will not occur. Completion of the heavy-duty equipment is highly susceptible to factors outside the entity's influence.

By the end of the first year, the entity has satisfied 65% of its performance obligation on the basis of costs incurred to date. Costs incurred to date are therefore ₹ 7,15,000 and S Limited reassesses the variable consideration and concludes that the amount is still constrained. Therefore at 31st March, 20X2, the following would be recognised:

Revenue (A)	– ₹ 13,00,000 (₹ 20,00,000 x 65%)
Costs (B)	– ₹ 7,15,000 (₹ 11,00,000 x 65%)
Gross profit (C) i.e.(A-B)	– ₹ 5,85,000

For the year 20X2-20X3

On 4th June, 20X2, the contract is modified. As a result, the fixed consideration and expected costs increase by ₹ 1,50,000 and ₹ 80,000, respectively.

The total potential consideration after the modification is ₹ 24,00,000 which is ₹ 21,50,000 fixed consideration + ₹ 2,50,000 completion bonus. In addition, the allowable time for achieving the bonus is extended by six months with the result that S Limited concludes that it is highly probable that including the bonus in the transaction price will not result in a significant reversal in the amount of cumulative revenue recognised in accordance with Ind AS 115. Therefore, the bonus of ₹ 2,50,000 can be included in the transaction price.

S Limited also concludes that the contract remains a single performance obligation. Thus, S Limited accounts for the contract modification as if it were part of the original contract. Therefore, S Limited updates its estimates of costs and revenue as follows:

S Limited has satisfied 60.60% of its performance obligation (₹ 7,15,000 actual costs incurred compared to ₹ 11,80,000 total expected costs). The entity recognises additional revenue of ₹ 1,54,400 [(60.60% of ₹ 24,00,000) – ₹ 13,00,000 revenue recognised to date] at the date of modification i.e. on 4th June, 20X2 as a cumulative catch-up adjustment.

6. (a) Extract of the Balance Sheet of RKA Private Ltd. as at 31st March, 20X2

	₹ in lacs
Closing net defined liability (1,580 – 1,275) lacs	305

Extract of the Statement of Profit or Loss of RKA Private Ltd. for the year ended 31st March, 20X2

Particulars	₹ in lacs
Service cost	55

Net interest (Refer W.N.1)	<u>21</u>
Profit or loss	76
Other comprehensive income:	
Remeasurements (Refer W.N.2)	<u>80</u>
Total	<u>156</u>

(b) **Journal entries in the books of RKA Private Ltd.**

Particulars		₹ in lacs	₹ in lacs
Profit & Loss	Dr.	76	
Other comprehensive income	Dr.	80	
To Cash (Contribution)			111
To Net defined benefit liability (Refer WN 3)			45

Working Notes:

1. Computation of Net interest taken to the Statement of Profit or Loss

= Discount rate x Opening net defined benefit liability

= 8% x (1,400 – 1,140) lacs

= 8% x 260 lacs = 21 lacs (Rounded off to nearest lacs)

2. Computation of Remeasurements

Defined Benefit Obligation Account

Particulars	₹ in lacs	Particulars	₹ in lacs
To balance c/d (given) (closing balance)	1,580	By balance b/d (given) (opening balance)	1,400
		By Current Service Cost (given)	55
		By Interest on Opening Liability (1,400 x 8%)	112
		By Actuarial loss (bal. figure)	<u>13</u>
	<u>1,580</u>		<u>1,580</u>

OR

Statement to calculate Actuarial gain or loss on defined benefit liability:

Particulars	₹ in lacs
Opening balance of liability	1,400
Current service cost	55
Interest on opening liability (1,400 x 8%)	112
Actuarial loss (Bal. fig)	<u>13</u>
Closing balance of liability	<u>1,580</u>

Plan Assets Account

Particulars	₹ in lacs	Particulars	₹ in lacs
To balance b/d (given) (opening balance)	1,140	By balance c/d (given) (closing balance)	1,275
To Bank Account (contribution for the year)	111		
To Surplus / Actual Return (bal. figure)	<u>24</u>		<u> </u>
	<u>1,275</u>		<u>1,275</u>

OR

Statement to calculate Actual return on plan assets:

Particulars	₹ in lacs
Opening balance of asset	1,140
Cash contribution	111
Actual return (Bal. fig)	<u>24</u>
Closing balance of asset	<u>1,275</u>

Net interest on opening balance of plan asset = ₹ 91 lacs (i.e. ₹ 1,140 lacs x 8%) (Rounded off to nearest lacs)

Hence there is a decrease in plan assets due to remeasurement for which computation is as follows:

Actual Return – Net interest on opening plan asset

= ₹ 24 lacs – ₹ 91 lacs = ₹ 67 lacs.

Net remeasurement would be computed as follows:

Actuarial loss on liability + Loss on return

= ₹ 13 lacs + ₹ 67 lacs = ₹ 80 lacs.

3. Computation of increase/ decrease in net defined benefit liability:

Particulars	₹ in lacs
Opening net liability (₹ 1,400 lacs – ₹ 1,140 lacs)	260
Closing net liability (₹1,580 lacs – ₹ 1,275 lacs)	<u>305</u>
Increase in liability	<u>45</u>

(b) Requirement as per Ind AS:

A first-time adopter shall classify all government loans received as a financial liability or an equity instrument in accordance with Ind AS 32. A first-time adopter shall apply the requirements in Ind AS 109 and Ind AS 20, prospectively to government loans existing at the date of transition to Ind AS and shall not recognise the corresponding benefit of the government loan at a below-market rate of interest as a government grant.

Treatment to be done:

Consequently, if a first-time adopter did not, under its previous GAAP, recognise and measure a government loan at a below-market rate of interest on a basis consistent with Ind AS

requirements, it shall use its previous GAAP carrying amount of the loan at the date of transition to Ind AS as the carrying amount of the loan in the opening Ind AS Balance Sheet. An entity shall apply Ind AS 109 to the measurement of such loans after the date of transition to Ind AS.

In the instant case, the loan meets the definition of a financial liability in accordance with Ind AS 32. Company therefore reclassifies it from equity to liability. It also uses the previous GAAP carrying amount of the loan at the date of transition as the carrying amount of the loan in the opening Ind AS balance sheet.

It calculates the annual effective interest rate (EIR) starting 1st April 2020 as below:

$EIR = \text{Amount} / \text{Principal}^{(1/n)}$ i.e. $2.50/2^{(1/4)}$ i.e. 5.74%. approx.

At this rate, ₹ 2 crore will accrete to ₹ 2.50 crore as at 31st March 2024.

During the next 4 years, the interest expense charged to statement of profit and loss shall be:

Year ended	Opening amortised cost (₹)	Interest expense for the year (₹) @ 5.74% p.a. approx.	Closing amortised cost (₹)
31 st March 2021	2,00,00,000	11,48,000	2,11,48,000
31 st March 2022	2,11,48,000	12,13,895	2,23,61,895
31 st March 2023	2,23,61,895	12,83,573	2,36,45,468
31 st March 2024	2,36,45,468	13,54,532	2,50,00,000

An entity may apply the requirements in Ind AS 109 and Ind AS 20 retrospectively to any government loan originated before the date of transition to Ind AS, provided that the information needed to do so had been obtained at the time of initially accounting for that loan.

The accounting treatment is to be done as per above guidance and the advice which the company has been provided is not in line with the requirements of Ind AS 101.

(c) Either

In the present case, Solar Limited controls Mars Limited (since it holds 80% of its voting rights). Consequently, it also controls the voting rights associated with 30% equity interest held by Mars Limited in Venus Limited. Solar Limited also has 25% direct equity interest and related voting power in Venus Limited. Thus, Solar Limited controls 55% (30% + 25%) voting power of Venus Limited. As the decisions concerning relevant activities of Venus Limited require a simple majority of votes. Solar Limited controls Venus Limited and should therefore consolidate it in accordance with Ind AS 110.

Although, Solar Limited controls Venus Limited, its entitlement to the subsidiary's economic benefits is determined on the basis of its actual ownership interest. For the purposes of the consolidated financial statements, Solar Limited's share in Venus Limited is determined as 49% [25% + (80% × 30%)]. As a result, 51% of profit or loss, other comprehensive income and net assets of Venus Limited shall be attributed to the non-controlling interests in the consolidated financial statements (this comprises 6% attributable to holders of non-controlling interests in Mars Limited [reflecting 20% interest of non-controlling shareholders of Mars Limited in 30% of Venus Limited] and 45% to holders of non-controlling interests in Venus Limited).

OR

In assessing whether it has obtained control over Company X, Company P should consider not only the 40,000 shares it owns but also its option to acquire another 25,000 shares (a so-called potential voting right). In this assessment, the specific terms and conditions of the option agreement and other factors are considered as follows:

- the options are currently exercisable and there are no other required conditions before such options can be exercised
- if exercised, these options would increase Company P's ownership to a controlling interest of over 50% before considering other shareholders' potential voting rights (65,000 shares out of a total of 1,25,000 shares)
- although other shareholders also have potential voting rights, if all options are exercised Company P will still own a majority (65,000 shares out of 1,29,000 shares)
- the premium included in the exercise price makes the options out-of-the-money. However, the fact that the premium is small and the options could confer majority ownership indicates that the potential voting rights have economic substance.

By considering all the above factors, Company P concludes that with the acquisition of the 40,000 shares together with the potential voting rights, it has obtained control of Company X.