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Further, in the Elective Papers which are Case Study based, the solutions have been worked out on the basis of certain assumptions/views derived from the facts given in the question or language used in the question. It may be possible to work out the solution to the case studies in a different manner based on the assumptions made or views taken.

PAPER – 6E: GLOBAL FINANCIAL REPORTING STANDARDS

*The question paper comprises **five** case study questions. The candidates are required to answer any **four** case study questions out of **five**.*

Case Study Question 1

Star Ltd. does business of manufacturing generator parts and generator sets for industrial and home use. They report their financial statements under International Financial Reporting Standards. While in the process of closing the books for the year ended 31st March, 2021, the Chief Financial Officer of the company identified a few transactions and asked for your assistance to show proper treatment.

On 1st April, 2020, Star Ltd purchased some land for ₹ 20 lakhs. Star Ltd. purchased the land in order to build a Plant for manufacturing generator parts. During the six months from 1st April, 2020 to 30th September, 2020, Star Ltd. incurred costs totaling ₹ 7 lakhs in preparing the land and erecting the structure of the Plant. This process caused some damage to the land for making it suitable for setting up the Plant. Star Ltd. began operations on 1st October, 2020 and the directors estimate that the Plant site would have useful economic life of 10 years from that date.

Star Ltd. is legally obliged to rectify the damage caused to the land for setting up the Plant. The directors estimate that the costs of this rectification after 10 years on 30th September, will be as follows:

- ₹ 6 lakhs to rectify the damage caused by the preparation of the land for setting up the Plant;

Following this rectification work the land could potentially be sold to a third party for no less than its original cost of ₹ 20 lakhs.

An annual discount rate appropriate for this project is 12%. The present value of ₹ 1 payable in 10 years' time with an annual discount rate of 12% is 32.2 paise. The present value of ₹ 1 payable in 9.5 years' time with an annual discount rate of 12% is 34.1 paise.

On 31st March, 2018, Star Ltd. purchased 80% of the equity of Galaxy Ltd. for ₹ 380 lakhs. The fair values of the net assets of Galaxy Ltd. that were included in the consolidated statement of financial position of Star Ltd. at 31st March, 2018 were measured at ₹ 400 lakhs (their fair values at that date). It is the group policy to value the non-controlling interest in subsidiaries at the date of acquisition at its proportionate share of the fair value of the subsidiaries' identifiable net assets.

On 31st March, 2021, Star Ltd. carried out its annual review of the goodwill on consolidation of Galaxy Ltd. for evidence of impairment. No impairment had been evident when the reviews were carried out on 31st March, 2019 and 31st March, 2020. The review involved allocating *the assets of Galaxy Ltd. into three cash-generating units and computing the value in use of each unit. The carrying values of the individual units before any impairment adjustments are given below:*

Particular	*Unit A ₹ in lakhs*	*Unit B ₹ in lakhs*	*Unit C ₹ in lakhs*
Intangible assets	*60*	*20*	*-*
Property, Plant and Equipment	*160*	*100*	*120*
Current Assets	*120*	*60*	*80*
Total	*340*	*180*	*200*
Value in use of unit	*360*	*132*	*208*

It was not possible to meaningfully allocate the goodwill on consolidation to the individual cash generating units but all the other net assets of Galaxy Ltd. are allocated in the table shown above.

The intangible assets of Galaxy Ltd. have no ascertainable market value but all the current assets have a market value that is at least equal to their carrying value. The value in use of Galaxy Ltd. as a single cash-generating unit on 31st March, 2021 is ₹ 700 lakhs.

On 1st December, 2020, Star Ltd. as a part of its expansion plan, opened a new Plant for manufacturing genset parts in an area designated by the government as an economic development area.

On that day, the government provided Star Ltd. with a grant of ₹ 60 lakhs to assist it in the development of the factory.

This grant was provided in three parts:

(i) ₹ 12 lakhs of the grant was a payment by the government as an inducement to Star Ltd. to begin developing the factory. No conditions were attached to this part of the grant.

(ii) ₹ 30 lakhs of the grant related to the construction of the factory at a cost of ₹ 120 lakhs. The land was leased so the whole of the ₹ 120 lakhs is depreciable over the estimated 40 year useful life of the factory.

(iii) The remaining ₹ 18 lakhs was received subject to keeping at least 200 employees working at the factory for a period of at least five years. If the number drops below 200 at any time in any financial year in this five year period, then 20% of the grant is repayable in that year.

From 1st December, 2020, 220 workers were employed at the factory and estimates are that this number is unlikely to fall below 200 over the relevant five year period.

Star·Ltd. planned the Plant under construction being financed through ₹ 16 lakhs of debt and of which ₹ 12 lakhs is a construction loan directly on the Plant. The rest is financed by the general debt of the company. Star Ltd. would put to use the Plant when it is completed.

The debt structure of Star Ltd. is as under:

Particular	₹ in lakhs
Construction Loan @ 11 %	₹ 12.00
Long term Debenture @ 9%	₹ 18.00
Long-term Subordinate Debenture @ 10%	₹ 6.00

The debentures and subordinated debentures were issued at the same time.

On 1st July, 2020, Star Ltd. decided to sell one of its divisions following a recent change in its geographical focus. The proposed sale would involve the buyer acquiring the non-monetary assets (including goodwill) of the division, with Star Ltd. collecting any outstanding trade receivables relating to the division and settling any current liabilities.

On 1st January, 2021, the carrying amounts of the relevant assets of the division were as follows:

- *Purchase goodwill ₹ 1.2 lakhs;*
- *Property, plant and equipment (average remaining estimated useful life two years) ₹ 4 lakhs;*
- *Inventories ₹ 2 lakhs.*

From 1st January, 2021, Star Ltd. began to actively market the division and has received a number of serious enquiries.

On 1st January, 2021, the directors estimated that they would receive ₹ 6.4 lakhs from the sale of the division. Since 1st January, 2021, market conditions have improved and on 30th April, 2021 Star Ltd. received and accepted a firm offer to purchase the division for ₹ 6.6 lakhs. The sale is expected to be completed on 30th June, 2021.

₹ 6.6 lakhs can be assumed to be a reasonable estimate of the value of the division on 31st March, 2021.

During the period from 1st January 2021 to 31st March, 2021, inventories of the division costing ₹ 1.6 lakhs were sold for ₹ 2.4 lakhs. At 31st March, 2021, the total cost of the inventories of the division was ₹ 1.8 Lakhs. All of these inventories have an estimated net realizable value that is in excess of their cost.

Further, on 1st January, 2021, Star Ltd. acquired 30% of the shares of Tara Ltd. The investment was accounted for as an associate in Star Ltd.'s consolidated financial statements.

Both Star Ltd. and Tara Ltd. have an accounting year end of 31st March, 2021. Star Ltd. has no other investments in associates.

Net profit for the year in Tara's income statement for the year ended 31st March, 2021 was ₹ 0.46 lakhs. It declared and paid dividend of ₹ 0.2 lakhs on 1st March, 2021. No other dividends were paid in the year.

I. Multiple Choice Questions

1.1 What would be the treatment for grant of ₹ 30 lakhs related to the construction of the factory at a cost of ₹ 120 lakhs?

(A) ₹ 30 lakhs grant in respect of the plant and equipment should be recognized immediately in the income statement, since the company is certain to build the factory.

(B) Deduct the grant received from the cost of the asset and depreciate the net carrying value over its useful economic life.

(C) Show the grant as a deferred credit and leave the initial carrying value of the property at ₹ 120 lakhs. Thereafter the deferred credit would be released to the income statement at the end of 40th year.

(D) Discount the grant and release after 40 years.

1.2 What would be the treatment of grant of ₹ 12 lakhs received from the government as an inducement to Star Ltd. to begin developing the factory?

(A) Grant relating to an inducement to begin developing the factory can be recognized immediately in the Statement of Profit or Loss.

(B) ₹ 0.30 lakhs amount is to be credited each year in the income statement over 40 year period.

(C) ₹ 2.4 lakhs amount is to be credited each year in the income statement over 40 year period.

(D) Net off the grant received against the cost of the asset and depreciate the net figure over its useful economic life.

1.3 What would be the treatment for grant of ₹ 18 lakhs which was received with a condition to keep at least 200 employees working at the factory?

(A) ₹ 1.2 lakhs would be recognized in the income statement for the current period ending 31st March, 2021.

(B) ₹ 3.6 lakhs would be recognized in the income statement for the current period ending 31st March, 2021.

(C) ₹ 18 lakhs would be recognized in the income statement for the period when at least 200 workers are employed in factory.

(D) ₹ 0.45 lakhs amount is to be credited each year in the income statement over 40 year period.

1.4 Changes to the deferred tax arising from business combination impacts:

(A) Statement of Profit or Loss

(B) Other Comprehensive Income

(C) Goodwill

(D) No changes - No impact

1.5 What amount will be shown as an inflow in respect of earnings from the associate in the statement of cash flows of Star Limited for the year ended 31st March, 2021?

(A) ₹ 0.040 lakhs

(B) ₹ 0.052 lakhs

(C) ₹ 0.060 lakhs

(D) ₹ 0.092 lakhs ***(2 Marks each i.e. 2 x 5 = 10 Marks)***

II. Descriptive Questions

1.6 What is the implication of rectification of damage of land mentioned in the case study? What is the relevant provision related to this concept under IFRS? ***(3 Marks)***

1.7 Show treatment of impairment of goodwill as per the details provided in the case study?

(4 Marks)

1.8 Based on the debt structure of the organization, calculate the following:

(a) total interest payable during the year ended 31st March, 2021

(b) the capitalized interest cost to be recorded as an asset in the Statement of Financial Position

(c) amount of interest expense to be reported on the income statement. ***(5 Marks)***

1.9 Explain the disclosure requirement related to sale of division and the treatment of property held for sale and discontinued operations? ***(3 Marks)***

Answer to Case Study 1

I. Answer to Multiple Choice Questions

1.1	Option (B)	Deduct the grant received from the cost of the asset and depreciate the net carrying value over its useful economic life
1.2	Option (A)	Grant relating to an inducement to begin developing the factory can be recognized immediately in the Statement of Profit or Loss
1.3	Option (A)	₹ 1.2 lakhs would be recognized in the income statement for the current period ending 31st March, 2021
1.4	Option (C)	Goodwill
1.5	Option (C)	₹ 0.060 lakhs

II. Answer to Descriptive Questions

1.6 In accordance with the principles of *IAS 16 'Property, Plant and Equipment',* costs of ₹ 27 lakhs (₹ 20 lakhs + ₹ 7 lakhs) will be debited to property, plant and equipment as cost of Plant.

From 1st October, 2020, an obligation exists to rectify the damage caused by the Plant and this obligation should be provided for.

The amount provided is the present value of the expected future payment, which is ₹ 1.932 lakhs (₹ 6 lakhs x 0.322).

The amount provided is debited to property, plant and equipment and credited to provision at 1st October, 2020.

The costs of Plant (excluding the land) will be ₹ 8.932 lakhs (₹ 7 lakhs + ₹ 1.932 lakhs).

This cost will be depreciated over a 10-year period, giving a charge in the current period of ₹ 0.447 lakhs in the current year (₹ 8.932 lakhs x 1/10 x 6/12).

The closing balance in property, plant and equipment is ₹ 28.485 lakhs (₹ 27 lakhs + ₹ 1.932 lakhs – ₹ 0.447 lakhs).

As the date of settlement of the liability draws closer the discount unwinds.

The unwinding of the discount in the current year is ₹ 0.116 lakhs (₹ 1.932 lakhs x 12% x 6/12).

The land rectification process itself creates an additional liability based on the damage caused by the reporting date.

The carrying amount of the provision at the year-end is ₹ 2.048 lakhs (₹ 1.932 lakhs + ₹ 0.116).

1.7 The goodwill on consolidation of Galaxy Ltd. that is recognized in the consolidated statement of financial position of Star Ltd. is ₹ 60 lakh (₹ 380 lakh – 80% x ₹ 400 lakh). This can only be reviewed for impairment as part of the cash generating units to which it relates. Since here the goodwill cannot be meaningfully allocated to the units, the impairment review is in two parts.

Values in use of Units A and C are more than their carrying values. However, the value in use of Unit B is less than its carrying amount. This means that the assets of unit B are impaired by ₹ 48 lakhs (₹ 180 lakhs – ₹ 132 lakhs). This impairment loss will be charged to the income statement.

Assets will be written down on a pro-rata basis as shown in the table below:

₹ in lakhs

Asset	**Impact on carrying value**		
	Existing	**Impairment**	**Revised**
Intangible assets	20	(8)	12
Property, plant and equipment	100	(40)	60
Current assets	60	Nil*	60
Total	180	(48)	132

* The current assets are not impaired because they are expected to realize at least their carrying value when disposed of.

Following this review, the three units plus the goodwill are reviewed together considering the recoverable amount of the business as a whole is ₹ 700 lakhs. **₹ in lakhs**

Component	**Impact of impairment review on carrying value**		
	Existing	**Impairment**	**Revised**
Goodwill (see below)	75	(47)	28
Unit A	340	Nil	340
Unit B	132	Nil	132
Unit C (revised)	200	Nil	200
Total	747	(47)	700

As per Appendix C of IAS 36, given that the subsidiary is 80% owned and NCI is computed as proportionate share of the subsidiary's fair value of net identifiable assets, the goodwill must first be grossed up to reflect a notional 100% investment. Therefore, the goodwill will be grossed up to ₹ 75 lakhs (₹ 60 lakhs x 100/80). The impairment loss of ₹ 47 lakhs is all allocated to goodwill, leaving the carrying values of the individual units of the business as shown in the table immediately above.

The table shows that the notional goodwill that relates to a 100% interest is written down by ₹ 47 lakhs to ₹ 28 lakhs. However, in the consolidated financial statements the goodwill that is recognized is based on an 80% interest so the loss that is actually recognized is ₹ 37.60 lakhs (₹ 47 lakhs x 80%) and the closing consolidated goodwill figure is ₹ 22.40 lakhs (₹ 28 lakhs x 80%) or (₹ 60 lakhs – ₹ 37.60 lakhs).

1.8 According to para 8 of IAS 23 "Borrowing Costs", an entity shall capitalize borrowing costs that are directly attributable to the acquisition, construction or production of a qualifying asset as part of the cost of that asset.

Other borrowing costs should be recognized as an expense in the period in which they are incurred.

Based on the above the treatment is as under:

(a) Calculation of total interest payable during the year ended 31st March, 2021:

11% of ₹ 12 lakhs + 9% of ₹ 18 lakhs +10% of ₹ 6 lakhs = ₹ 3.54 lakhs

(b) Capitalized interest cost to be added to the cost of the asset in the Statement of Financial Position:

Capitalisation rate = [{(₹ 18 lakhs/ ₹ 24 lakhs) x 9%} + {(₹ 6 lakhs / ₹ 24 lakhs) x 10%}] x 100

= 9.25%

Capitalized interest cost would be

= [(₹ 12 lakhs x 11%) + (₹ 4 lakhs x 9.25%)]

= ₹ 1.32 lakhs + ₹ 0.37 lakhs

= ₹ 1.69 lakhs

(c) Amount of interest expense to be reported in the Income Statement:

= ₹ 3.54 lakhs – ₹ 1.69 lakhs

= ₹ 1.85 lakhs

1.9 The decision to offer the division for sale on 1st January, 2021 means that from that date the division is classified as held for sale. The division available for immediate sale, is being actively marketed at a reasonable price, and the sale is expected to be completed within one year.

The consequence of this classification is that the assets of the division will be measured at the lower of their existing carrying amounts (₹ 7.20 lakhs) and their fair value less costs to sell (6.40 lakhs). This means measuring the assets of the division at ₹ 6.40 lakhs on 1st January, 2021.

The reduction in carrying value of the assets of ₹ 0.80 lakhs (₹ 7.20 lakhs – ₹ 6.40 lakhs) will be treated as an impairment loss and allocated to goodwill, leaving a carrying amount for goodwill of ₹ 0.40 lakhs (₹ 1.20 lakhs – ₹ 0.80 lakhs).

The increased expectation of the selling price of ₹ 0.20 lakhs (₹ 6.60 lakhs – ₹ 6.40 lakhs) will be treated as a reversal of an impairment loss. However, since this reversal relates to goodwill, it cannot be recognised.

The assets of the division need to be presented separately from other assets in the statement of financial position. Their major classes of assets classified as held for sale should be separately disclosed, either in the statement of financial position or in the notes.

The property, plant and equipment should not be depreciated after 1st January, 2021, so it's carrying value at 31st March, 2021 will be ₹ 4 lakhs. The inventories of the division will be shown at their year-end cost of ₹ 1.80 lakhs.

The division will be regarded as a discontinued operation for the year ended 31st March, 2021. It represents a separate line of business and is held for sale at the year end.

The statement of comprehensive income should disclose, as a single amount, the post-tax profit or loss of the division and the impairment loss arising on the re-measurement of the division on classification as held for sale. Further analysis of this single amount may be presented in the notes or in the statement of comprehensive income. If it is presented in the statement of comprehensive income it shall be presented in a section identified as relating to discontinued operations, i.e. separately from continuing operations.

Case Study Question 2

EARTH Limited is an IFRS compliant multinational company which is engaged in various businesses. PLUTO Limited, a subsidiary of EARTH Limited, also follows IFRS for its financial reporting and is engaged in the business of consultation for civil engineering projects such as highways, buildings, etc. On 1st April, 2021, PLUTO Limited won a contract to provide consultancy to the Government in relation to a highway project. Following are the salient features of the contract:

- *Total period for which PLUTO Limited is required to provide consultancy is 2 years starting from 1st April, 2021.*

- *Total consultancy fees to be received by PLUTO Limited during the contract period is ₹ 50 crore.*
- *On 1st April, 2021, EARTH Limited will be required to provide a performance guarantee to the Government for an amount up to ₹ 50 crore. If the consultancy services provided by PLUTO Limited is not satisfactory, the Government can invoke the performance guarantee. If the guarantee is invoked, EARTH Limited will be required to indemnify the Government for the loss suffered because of non-satisfactory performance by PLUTO Limited.*

To execute the project, on 1st April, 2021, PLUTO Limited has availed a short-term loan of ₹ 30 crore from the bank with the following covenants:

- *EARTH Limited shall provide a financial guarantee for an amount up to ₹ 30 crore.*
- *If PLUTO Limited makes any default on repayment of the loan, EARTH Limited will be required to indemnify the bank up to an amount of ₹ 30 crore.*

For providing the above-mentioned two guarantees, EARTH Limited has charged commission from PLUTO Limited at the market rate of 1% of the guaranteed amount applicable to such guarantees. As per the revenue recognition policy of EARTH Limited, it has decided to recognize the guarantee commission income in profit or loss over a period of two years (term of the contract) starting from 1st April, 2021 using the straight-line method.

Based on the performance and credit history of PLUTO Limited, the management of EARTH Limited has established that there is no need to recognize any impairment allowance. The CFO of EARTH Limited is of the opinion that both the guarantees given should not be recognized in the balance sheet of EARTH Limited. However, she believes that these guarantees should be disclosed as contingent liabilities in the notes to the financial statements.

Following is the summarized statement of profit or loss of EARTH Limited as per IFRS for the year ended 31st March, 2022:

Particulars		*₹ in crore*
Revenue from operations		*1,160.00*
Other income		*56.00*
Total Income	*(A)*	*1,216.00*
Purchase of stock-in-trade		*40.00*
Changes in inventories of stock-in-trade		*6.00*
Employee benefits expense		*116.00*
Finance costs		*130.00*
Depreciation and amortization expense		*30.00*

Other expenses		*300.00*
Total Expenses	*(B)*	*622.00*
Profit Before Tax	*(C=A-B)*	*594.00*
Current tax		*165.40*
Deferred tax		*1.50*
Tax Expenses	*(D)*	*166.90*
Profit after Tax	*(C-D)*	*427.10*

Additional information:

- *Corporate income tax rate applicable to EARTH Limited is 30%.*
- *Other income includes long-term capital gains of ₹ 10 crore which are taxable at the rate of 10%.*
- *Other expenses include the following items which are not deductible for income tax purposes:*

Item	*₹ in crore*
Penalties	*1.00*
Impairment of goodwill	*44.00*
Corporate Social Responsibility expense	*6.00*

- *Other expenses include research and development (R & D) expenditure of ₹ 8 crore in respect of which a 200% weighted deduction is available under income tax laws.*
- *Other income includes dividends of ₹ 4 crore, which is exempt from tax.*
- *Profit before tax of ₹ 594 crore includes*
  (i) agriculture income of ₹ 55 crore which is exempt from tax; and
  (ii) profit of ₹ 60 crore earned in the USA on which EARTH Limited has paid tax at the rate of 20%.
- *Depreciation as per income tax laws is ₹ 25.0 crore.*

During review of the financial statements of EARTH Limited, the CFO multiplied profit before tax by the income tax rate and arrived at ₹ 178.2 crore as the tax expense (₹ 594 crore x 30% = ₹ 178.2 crore). However, actual income tax expense appearing in the summarized statement of profit and loss is ₹ 166.9 crore.

Other information:

On 1st April, 2021, EARTH Ltd. issues a new instrument with the following characteristics:

- *Face value 100, issue price 90.*

- *Cumulative dividend payable at 5% per annum for 10 years. After 10 years, the dividend is payable at the discretion of the issuer.*
- *The holder of the note has the option to convert into ordinary shares of EARTH Ltd. after 10 years, and conversion will be 10 ordinary shares for each instrument.*
- *The holder can demand redemption for the face value at any time, with six months' notice up until the end of 10 years. After 10 years, redemption is at the discretion of the issuer.*
- *There is no fixed maturity date.*

S Limited is a subsidiary of H Limited which is an associate of T Ltd. T Ltd. is an associate of EARTH Limited. S Limited's functional and presentation currency is INR, while the functional currency of its parent is USD and its presentation currency is EUR. S Limited has a firm commitment to buy a commodity in EUR. It has entered into a forward contract to hedge the firm commitment against foreign exchange risk. It has to prepare its financial statements for the purpose of consolidation with its parent.

EARTH Limited is a huge machine manufacturer. It has to overhaul its machinery every 3 years. It has purchased machinery worth ₹ 1,00,00,000. It is estimated that the overhaul costs will be ₹ 10,00,000. It is expected that the machine has a useful life of 10 years.

I. Multiple Choice Questions

2.1 How should the instrument be classified by EARTH Ltd. in the first 10 years in accordance with IAS 32? Select which one of the following is correct.

(A) As an equity

(B) As a liability

(C) Either as an equity or a liability

(D) As a compound instrument

2.2 How can S Limited account for a hedge relationship for the purpose of preparing H Limited's consolidated financial statements?

(A) Cash flow hedge

(B) Fair value hedge

(C) Option to designate under cash flow hedge or fair value hedge

(D) Net investment hedge

2.3 How should EARTH Limited initially recognize the purchase of its machinery?

(A) Recognize the machine at its cost of ₹ 1,00,00,000 and depreciate over 10 years

(B) Recognize two assets - the machine worth ₹ 90,00,000 to be depreciated over 10 years and costs related to overhaul of ₹ 10,00,000 to be depreciated over 3 years

(C) Recognize two assets - the machine worth ₹ 1,00,00,000 to be depreciated over 10 years and costs related to overhaul of ₹ 10,00,000 to be depreciated over 3 years

(D) Recognize an asset for ₹ 90,00,000 to be depreciated over 10 years and expense ₹ 10,00,000 immediately.

2.4 A company prepares segment information for its management reporting purposes. Under IFRS 8 'Operating Segments', the company can also use this segment information to determine the appropriate segments for financial reporting. Applying this approach, which of these are the company's reportable segments under IFRS 8?

(A) Segments deemed significant by the management and are reviewed regularly by them

(B) Segment whose information is presented by the company's industry peers

(C) Each segment whose operating results are reviewed regularly by the Board of directors of the company to make decisions about resources to be allocated to the segment

(D) Each segment whose operating results are reviewed regularly by the Managing Director who is the chief operating decision maker to make decisions about resources to be allocated to the segment.

2.5 Which of the following is incorrect in respect of a statement of cash flows under IFRS?

(A) The cash flow effects of disposals cannot be deducted from those of acquisitions

(B) Cash payment to the shareholders for buying back its shares is a financing activity

(C) An entity only includes the transactions between itself and the joint venture when preparing the consolidated statement of cash flows

(D) Non-cash investing and financing transactions are to be disclosed as part of the statement of cash flows. ***(2 Marks each i.e. 2 x 5 = 10 Marks)***

II. Descriptive Questions

2.6 Comment on the accounting and disclosure principles proposed by the CFO in respect of each of the guarantees. ***(4 Marks)***

2.7 Provide necessary journal entries, if any, as on 1st April, 2021, and 31st March, 2022 in the books of EARTH Limited. ***(4 Marks)***

2.8 The CFO has sought your help in reconciling the difference between the two tax expense amounts. Prepare a reconciliation containing the disclosure as required under the relevant IFRS. ***(7 Marks)***

Answer to Case Study 2

I. Answer to Multiple Choice Questions

2.1 Option (B) : As a liability

2.2 Option (C) : Option to designate under cash flow hedge or fair value hedge

2.3 Option (B) : Recognize two assets – the machine worth ₹ 90,00,000 to be depreciated over 10 years and costs related to overhaul of ₹ 10,00,000 to be depreciated over 3 years.

2.4 Option (D) : Each segment whose operating results are reviewed regularly by the Managing Director who is the chief operating decision maker to make decisions about resources to be allocated to the segment.

2.5 Option (D) : Non-cash investing and financing transactions are to be disclosed as part of the cash flow statement.

II. Answer to Descriptive Questions

2.6 Accounting and disclosure of performance guarantee and financial guarantee:

1. Performance Guarantee

Performance guarantee relates to satisfactory performance of the subsidiary to the Government for the consultancy on highway project. Since PLUTO Ltd. has good performance and credit history, CFO of EARTH Ltd. correctly opine that there is no need to recognise such guarantee as liability in the books of EARTH Ltd. However, the entity may apply IAS 37 to determine whether it meets the criteria to be disclosed as a contingent liability in its financial statements. Hence, in this case the view of CFO is correct.

2. Financial Guarantee

Since financial guarantee is in relation to a debt instrument (it is in relation to the loan taken by PLUTO Limited), it fulfils the definition of a financial guarantee. Accordingly, EARTH Limited shall apply IFRS 9 to recognize and measure the financial guarantee in its financial statements. Therefore, the views expressed by CFO is not in line with IFRS.

A financial guarantee contract is initially recognized at fair value. If the guarantee is issued on a commercial basis, the initial fair value is likely to equal the premium received.

Subsequently, at the end of the reporting period, financial guarantee will be measured at the higher of:

- The amount of the loss allowance, and
- The amount initially recognised less cumulative amortisation, where appropriate.

As the loss allowance is expected to be zero and the guarantee being for not more than 12 months, EARTH Ltd. shall derecognise the guarantee liability of ₹ 0.30 crore and recognise guarantee commission income of ₹ 0.30 crore.

The contention of CFO is wrong because paragraph 2 of IAS 37, 'Provisions, Contingent Liabilities and Contingent Assets', states that it does not apply to financial instruments (including guarantees) that are within the scope of IFRS 9, 'Financial Instruments'. Therefore, disclosure of financial guarantees as contingent liabilities is neither in accordance with IFRS 9 nor in accordance with IAS 37.

2.7 Journal Entries in the books of EARTH Ltd.:

(i) **With respect to performance guarantee:**

1st April, 2021

Cash/Bank A/c (50 crore x 1%)	Dr.	0.50 crore	
To Deferred Commission income			0.50 crore
(Being commission received)			

<u>31st March, 2022</u>

Deferred Commission income (0.50 crore / 2 years)	Dr.	0.25 crore	
To Commission income - Profit and Loss			0.25 crore
(Being commission income recognised in profit and loss over the two-year period on Straight Line basis)			

(ii) **With respect to financial guarantee:**

Initial Measurement (1st April, 2021):

Investment in PLUTO Ltd. (Subsidiary)/(Cash/bank)	Dr.	0.30 crore	
To Financial guarantee liability			0.30 crore
(Being guarantee initially recorded)			

Subsequent Measurement (31st March, 2022):

Subsequent recognition of commission income as it is a short-term loan

Financial guarantee liability	Dr. 0.30 crore	
To Commission income		0.30 crore

(Being guarantee liability subsequently reversed on completion and commission income recognised)

2.8 Reconciliation of income tax expense and current tax as per accounting profit for the year ended 31st March, 2022

Particulars		**₹ in crore**
Accounting profit		594.00
Tax at the applicable tax rate of 30%		178.20
Tax effect of expenses that are not deductible in determining taxable profits:		
Penalties (1.00 x 30%)	0.30	
Impairment of goodwill (44.00 x 30%)	13.20	
Corporate social responsibility expense (6.00 x 30%)	1.80	15.30
Tax effect of expenses that are deductible in determining taxable profits:		
Research and development expenses (8.00 x 30%)		(2.40)
Tax effect of income that are exempted in determining taxable profits:		
Dividend income (Exempt) (4.00 x 30%)	1.20	
Agriculture income (Exempt) (55.00 x 30%)	16.50	(17.70)
Tax effect of income on which different tax rates are used for determining taxable profits:		
Differential income tax on long term capital gain [10.00 x (30% - 10%)]	2.00	
Foreign income in USA [60.00 x (30%-20%)]	6.00	(8.00)
Income tax expense (Current) reported in the Statement of Profit and Loss for the current year		165.40

Reconciliation of deferred tax:

Particulars	₹ in crore
Deferred tax in relation to depreciation and amortization on property, plant and equipment and intangible assets [(30 – 25) x 30%]	1.50
Tax expense (deferred) reported in the Statement of Profit or Loss for the current year	1.50

Case Study Question 3

Princess Ltd. is manufacturing readymade garments and it is having branches throughout India.

Princess Ltd. acquires 60% of the equity shares of Dude Ltd. a private entity, for ₹ 48.75 crore during the year. The fair value of its identifiable net assets is ₹ 75 crore. The fair value of 40% of ordinary shares owned by non-controlling shareholders is ₹ 32.5 crore. Carrying amount of Dude Ltd.'s net assets is ₹ 60 crore.

On 1st April, 2020, a 8% convertible loan with a nominal value of ₹ 6,00,000 was issued at par. It is redeemable on 31st March, 2024 also at par. Alternatively, it may be converted into equity shares on the basis of 100 new shares for each ₹ 200 worth of loan.

An equivalent loan without the conversion option would have carried interest at 10%. Interest of ₹ 48,000 has already been paid and included as a finance cost. (PVF Year 1 : 0.91; Year 2 : 0.83: Year 3: 0.75; Year 4: 0.68. The amount to be recognized as liability is to be rounded off to the nearest thousand.)

On 1st April, 2020, the fair value of the assets of Princess Ltd.'s defined benefit plan were valued at ₹ 10,20,000 and the present value of the defined obligation was ₹ 10,62,500. On 31st March, 2021, the plan received contributions from Princess Ltd. amounting to ₹ 2,12,500 and paid out benefits of ₹ 1,27,500. The current service cost for the financial year ending 31st March, 2021 is ₹ 2,55,000. An interest rate of 5% is to be applied to the plan assets and obligations. The fair value of the plan's assets at 31st March, 2021 was ₹ 11,90,000, and the present value of the defined benefit obligation was ₹ 13,60,000.

Princess Ltd. has the policy that it will rectify the manufacturing defects if any or replace the defected goods with fresh garments if they are reported within three months of purchase.

If minor defects were detected in all products sold, repair costs of ₹ 2 million would result. If major defects were detected in all products sold, repair costs of ₹ 6 million would result. The company's past experience and future expectations indicate that, for the coming year, 85% of the goods sold will have no defects, 10% of the goods sold will have minor defects and 5% of *the goods sold will have major defects. In accordance with the standard, the company assesses the probability of an outflow for the warranty obligations as a whole.*

On 1st January, 2021, Princess Ltd. notified that a customer R was taking legal action against the company in respect of a financial losses incurred by the customer R. Customer R alleged that the financial losses were caused due to supply of faulty products on 31st October, 2020 by the Company. Princess Ltd. defended the case but considered, based on the progress of the case up to 31st March, 2021, that there was an 80% probability they would have to pay damages of ₹ 20 lakhs to the customer R.

However, the accountant of Princess Ltd. has not recorded this transaction in its financial statement as the case is not yet finally settled. The case was ultimately settled against the company resulting into payment of damages of ₹ 25 lakhs to the customer R on 15th May, 2021. The financials have been authorized by the Board of Directors in its meeting held on 18th May, 2021.

Princess Ltd. issued 12% Debentures worth ₹ 3,00,00,000 to fund the construction of Administrative Block on 1st July, 2020 but the development activities has yet to be started. On 1st April, 2020, Princess Ltd. began the construction of a Plant being qualifying asset using the existing borrowings. Expenditure drawn down for the construction was: ₹ 75,00,000 on 1st April, 2020 and ₹ 3,75,00,000 on 1st January, 2021.

Princess Ltd. also had the following loans in place at the end of 31st March, 2021:

(Amounts in '000)

Loan	1st April, 2020	31st March, 2021
18% Bank Loan	15,000	15,000
16% Term Loan	45,000	45,000
12% Debentures	-	30,000

I. Multiple Choice Questions

3.1 *What will be the Goodwill, when non-controlling interests are measured at fair value?*

(A) ₹ 6.25 crore

(B) ₹ 11.25 crore

(C) ₹ 15.0 crore

(D) ₹ 26.25 crore

3.2 What will be the Goodwill, when non-controlling interests are measured at proportionate share of identifiable net assets?

(A) ₹ 2.5 crore

(B) ₹ 3.75 crore

(C) ₹ 6.25 crore

(D) ₹ 11.0 crore

3.3 The borrowing cost that can be capitalized for the plant should be

(A) ₹ 27,84,375

(B) ₹ 42,75,000

(C) ₹ 53,43,750

(D) ₹ 74,25,000

3.4 The expected value of the cost of repairs is

(A) ₹ 7,00,000

(B) ₹ 5,00,000

(C) ₹ 4,50,000

(D) ₹ 4,00,000

3.5 The capitalization rate for the plant is

(A) 4.5%

(B) 12.0%

(C) 16.5%

(D) 17.25% ***(2 Marks each i.e. 2 x 5 = 10 Marks)***

II. Answer to Descriptive Questions

3.6 Analyze whether the accounting treatment made by the accountant, in case of customer R is in compliance with the IFRS. If not, advise the correct treatment along with working for the same. ***(5 Marks)***

3.7 Provide reconciliation from the opening balance to the closing balance for Plan assets and Defined benefit obligation. Also show how much amount should be recognized in the statement of profit or loss, other comprehensive income and balance sheet?

(5 Marks)

3.8 *Explain how will the Company account for the above loan notes in the financial statements for the year ended 31st March, 2021?*

Present value rates are:

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

(5 Marks)

Answer to Case Study 3

I. Answer to Multiple Choice Questions

3.1 Option (A) : ₹ 6.25 crore

3.2 Option (B) : ₹ 3.75 crore

3.3 Option (A) : ₹ 27,84,375

3.4 Option (B) : ₹ 5,00,000

3.5 Option (C) : 16.5%

II. Answer to Descriptive Questions

3.6 In accordance with IAS 37 'Provisions, Contingent Liabilities and Contingent Assets' the claim made by the customer R needs to be recognised as a liability in the financial statements for the year ended 31st March 2021.

The standard stipulates that a provision should be made when, at the reporting date:

– An entity has a present obligation arising out of a past event

– There is a probable outflow of economic benefits

– A reliable estimate can be made of the outflow

Since, all three of the above conditions are satisfied here, a provision is required to be made.

The provision should be measured at the amount the entity would rationally pay to settle the obligation at the reporting date.

In the given case even though the case is not finalized on the reporting date yet based on the progress of the case till reporting date, there is 80% probability to pay the damages. Further, reliable estimate of the amount which the entity is likely to incur can also be measure. Therefore, the treatment provided by the company of not recording the provision is not correct.

Princess Ltd. is required to make provision for the claim from customer R as per IAS 37 since the claim is a present obligation as a result of delivery of faulty products. Also, it is probable that an outflow of resources embodying economic benefits will be required to settle the obligations. Further, a reliable estimate of ₹ 20 lakhs can be made of the amount of the obligation while preparing the financial statements as on 31st March, 2021. Hence, a provision of ₹ 20 lakhs will be made with a corresponding charge to profit or loss.

However, following the principles of IAS 10, evidence of settlement amount is an adjusting event. Therefore, the amount of provision shall be increased to ₹ 25 lakhs and accordingly the same will be recognized as current liability.

3.7 Reconciliation of Plan assets and Defined benefit obligation

	Plan Assets ₹	Defined benefit obligation ₹
Fair value/present value as at 1st April, 2020	10,20,000	10,62,500
Interest @ 5%	51,000	53,125
Current service cost	-	2,55,000
Contributions received	2,12,500	-
Benefits paid	(1,27,500)	(1,27,500)
Return on plan assets (gain) (balancing figure)	34,000	-
Actuarial Loss (balancing figure)	-	1,16,875
Closing balance as at 31st March, 2021	11,90,000	13,60,000

In the Statement of Profit or loss, the following will be recognised:	**₹**
Current service cost	2,55,000
Net interest on net defined liability (₹ 53,125 – ₹ 51,000)	2,125

Defined benefit re-measurements recognised in Other Comprehensive Income:

	₹
Loss on defined benefit obligation	(1,16,875)
Gain on plan assets	34,000
	(82,875)

In the Balance sheet, the following will be recognised :	**₹**
Net defined liability (₹ 13,60,000 – ₹ 11,90,000)	1,70,000

3.8 The instrument contains both a liability (for payment of interest and nominal value of loan) and an equity component (in case of conversion of nominal value of loan into equity shares).

From the perspective of the entity, on evaluation of the terms and conditions of the financial instrument, it is determined that the instrument (8% convertible loan) comprises of two components:

- A financial liability (a contractual arrangement to deliver cash or another financial asset); and
- An equity instrument (an option granting the holder the right, for a specified period of time, to convert it into a fixed number of ordinary shares of the entity).

In the given case, the debt instrument can be redeemed at par on maturity date i.e. 31st March, 2024 and also the instrument gives an option to the holder to convert the amount into equity shares on maturity date, hence, it is a compound instrument.

Accordingly, an entity recognises separately the components of a financial instrument that

(a) creates a financial liability of the entity and

(b) grants an option to the holder of the instrument to convert it into an equity instrument of the entity.

Computation of Equity and Debt Component of 8% convertible loan as on 1st April, 2020

	₹
Present value of the principal repayable after four years	4,08,000
[6,00,000 x 0.68 (using 10% Discounting factor)]	
Add: Present value of Interest	
[(6,00,000 x 8%) x (0.91+0.83+0.75+0.68) (4 years cumulative 10% discounting factor)]	1,52,160
Value of debt component	5,60,160
Value of equity component (balancing figure)	39,840
Proceeds of the issue	6,00,000

Journal Entry

	Dr. (₹)	Cr. (₹)
At the inception date i.e. 1st April, 2020		
Bank A/c Dr.	6,00,000	
To 8% Convertible loan (Liability component) A/c		5,60,160
To 8% Convertible loan (Equity component) A/c		39,840
(Being 8% convertible loan bifurcated into liability and equity component at initial date)		

Further, on subsequent reporting date i.e. 31st March, 2021 the outflow of interest of ₹ 48,000 (6,00,000 x 8%) is not a finance cost as the effective interest rate for computation of finance cost on convertible loan is 10%. Hence, finance cost should be 5,60,160 x 10% = 56,016.

Closing balance of liability component on 31st March, 2021 would be ₹ 5,60,160 + 56,016 – 48,000 = 5,68,176.

Therefore, following rectified journal entry will be passed on 31st March, 2021:

Journal entry

	Dr. (₹)	Cr. (₹)
At the reporting date i.e. 31st March, 2021		
Finance cost (56,016 – 48,000) Dr.	8,016	
To 8% Convertible loan (Liability component) A/c		8,016
(Being deficit in finance cost recognised by corresponding credit to loan account- liability component)		

Journal entries

	Dr. (₹)	Cr. (₹)
At the reporting date i.e. 31st March, 2021		
8% Convertible loan (Liability component) A/c Dr.	48,000	
To Finance cost		48,000
(Being reversal of wrong amount of finance cost)		
Finance cost Dr.	56,016	
To 8% Convertible loan (Liability component) A/c		56,016
(Being correct amount of finance cost @ 10% recorded in the books)		

Case Study Question 4

Delicious Ltd. is manufacturing and selling 'Prepared Foods' and 'Packed Snacks'. It domiciled in India with its registered office situated at Shivajinagar, Pune and its manufacturing facility near Pune. The Company has been incorporated under the provisions of the Indian Companies Act and its equity shares are listed on the Bombay Stock Exchange Limited and the National Stock Exchange Limited.

On 1st April, 2021, Delicious Ltd. entered into a contract to purchase goods from Best Ltd. and agreed that the contract will be settled by issuing equity instruments of Delicious Ltd. Delicious Ltd. received the goods on 30th July, 2021. The share-based payment transaction was measured based on the fair value of the equity instruments as on 1st April, 2021.

Delicious Ltd. has entered into a contract with Dena Ltd. Dena Ltd. will supply Delicious Ltd., with a range of services. The payment for those services will be in cash and based upon the price of Delicious Ltd.'s ordinary shares on completion of the contract.

Delicious Ltd. has identified the following business components:

Segment	Revenue (₹)		Profit (₹)	Assets (₹)
	Internal	External		
A	1,00,000	1,00,000	1,25,000	12,50,000
B	NIL	48,50,000	10,00,000	22,50,000
C	25,000	1,25,000	1,00,000	2,00,000
D	20,50,000	4,00,000	2,75,000	3,00,000
Total for the entity*	22,50,000*	54,00,000*	15,00,000	45,00,000*

Delicious Ltd. identified some assets and liabilities as disposal group and plans to sell that group of assets and liabilities on 1st June, 2021. On 31st July, 2021, the Board of Directors approves and becomes committed to the plan to sell the manufacturing unit by entering into a firm purchase commitment with Royal Ltd. However, since the manufacturing unit is regulated, the approval from the regulator is needed for sale. The approval from the regulator is customary and highly probable to be received by 30th November, 2021 and the sale is expected to be completed by 31st March, 2022. Delicious Ltd. follows December year end.

***PS:** Read total of internal revenue as '₹ 21,75,000' instead of '₹ 22,50,000'; Total of external revenue as '₹ 54,75,000' instead of '₹ 54,00,000' and total assets as '₹ 40,00,000' instead of '₹ 45,00,000'.

The assets and liabilities attributable to this manufacturing unit are as under: ***(Amount in ₹)***

Particulars	Carrying value as on 31st December, 2020	Carrying value as on 31st July, 2021
Goodwill	300	300
Plant and Machinery	500	450
Building	1,000	925
Debtors	425	525
Inventory	350	200
Creditors	(150)	(125)
Loans	(1,000)	(925)
	1,425	1,350

The fair value of the manufacturing unit as on 31st December, 2020 is ₹ 1,000 and as 31st July, 2021 is ₹ 925. The cost to sell is ₹ 50 on both these dates. The disposal groups are not sold at the period end i.e., 31st December, 2021. The fair value as on 31st December, 2021 is lower than the carrying value of the disposal group as on that date.

Also, Delicious Ltd. re-valued the packing plant from ₹ 1 crore to ₹ 1.5 crore and created a deferred tax liability of ₹ 5 lakh. But the accountant didn't record this in the accounts.

Delicious Ltd. imported a cooler plant for ₹ 75,00,000 on 15th July, 2021 and was expected to reach the premises on 15th November, 2021. Due to some uncontrollable events, the machinery was delivered on 20th December, 2021. Due freight charges were paid. While this was happening, Delicious Ltd. was informed from the bank that it was being charged interest on the loan it had taken to fund the cost of the plant.

From the following particulars, the company wants to find out the net defined benefit liability.

(₹ in lakhs)

Particulars	Defined benefit obligation		Plan Assets	
	31st Dec. 2021	31st Dec. 2020	31st Dec. 2021	31st Dec. 2020
Balance at the beginning of the year	63.25	47.08	21.80	14.65
Current service cost	5.84	4.97	-	-
Interest cost	4.27	3.56	-	-
Changes in demographic assumptions	0.62	1.86	-	-
Changes in financial assumptions	3.58	1.93	-	-

Experience variance	*(2.49)*	*4.46*	*-*	*-*
Benefits paid	*-*	*(0.61)*	*-*	*(0.61)*
Investment income	*-*	*-*	*1.47*	*1.12*
Employers' contribution	*-*	*-*	*8.00*	*7.00*
Return on plan assets	*-*	*-*	*2.12*	*(0.35)*

I. Multiple Choice Questions

4.1 What is the measurement date in the agreement between Delicious Ltd. and Best Ltd.?

(A) 1st April, 2021

(B) 30th April, 2021

(C) 30th July, 2021

(D) 1st July, 2021

4.2 Which out of the following is the correct accounting treatment for the deferred tax liability?

(A) Debit statement of profit and loss by ₹ 5 lakhs

(B) Debit packing plant by ₹ 5 lakhs

(C) Debit other comprehensive income (revaluation reserve) by ₹ 5 lakhs.

(D) Debit deferred tax assets by ₹ 5 lakhs

4.3. In case of cooler plant, what is the proper treatment of freight and interest expense?

(A) Both expenses should be capitalized

(B) Freight charges should be capitalized and interest cannot be capitalized.

(C) Interest may be capitalized and freight should be expensed

(D) Both expenses should be expensed.

4.4 The company shall recognize the impairment loss for any or subsequent write down of the asset to

(A) Nominal value

(B) Carrying amount

(C) Carrying amount less cost to sell

(D) Fair value less cost to sell.

4.5 *In accordance with IFRS 2 'Share-based Payment', what type of share-based payment transaction with Dena Ltd. represents?*

(A) *Equity-settled share-based payment transaction*

(B) *Asset-settled share-based payment transaction*

(C) *Liability-settled share-based payment transaction*

(D) *Cash-settled share-based payment transaction*

(2 Marks each i.e. 2 x 5 = 10 Marks)

II. Descriptive Questions

4.6 *Which of the segments would be reportable as per the criteria prescribed in IFRS 8?* ***(4 Marks)***

4.7 (i) *Assess whether the manufacturing unit can be classified as held for sale and reasons there for. If yes, then at which date?* ***(3 Marks)***

(ii) *The measurement of the manufacturing unit as on the date of classification as held for sale.* ***(3 Marks)***

4.8 *Find out the net defined benefit liability and calculate the expense to be recognized in Profit and Loss account.* ***(5 Marks)***

Answer to Case Study 4

I. Answer to Multiple Choice Questions

4.1 Option (C) : 30th July, 2021

4.2 Option (C) : Debit other comprehensive income (revaluation reserve) by ₹ 5 lakhs

4.3 Option (B) : Freight charges should be capitalized and interest cannot be capitalized

4.4 Option (D) : Fair value less cost to sell

4.5 Option (D) : Cash-settled share-based payment transaction

II. Answer to Descriptive Questions

4.6 An entity should report separately information about an operating segment that meets any of the following quantitative thresholds:

(a) Its reported revenue, including both sales to external customers and inter-segment sales or transfers, is 10% or more of the combined revenue, internal and external, of all operating segments.

(b) The absolute amount of its reported profit or loss is 10% or more of the greater, in absolute amount, of

(i) the combined reported profit of all operating segments that did not report a loss and

(ii) the combined reported loss of all operating segments that reported a loss.

(c) Its assets are 10% or more of the combined assets of all operating segments.

Operating segments that do not meet any of the quantitative thresholds may be considered reportable and separately disclosed, if management believes that information about the segment would be useful to users of the financial statements.

Further, if the total external revenue reported by operating segments constitutes less than 75% of the entity's revenue, additional operating segments should be identified as reportable segments (even if they do not meet the criteria) until at least 75% of the entity's revenue is included in reportable segments.

Determination of Reportable Segments following quantitative thresholds criteria:

Segments	**A**	**B**	**C**	**D**	**Reportable Segments**
% Segment sales to total sales	2.61%	63.40%	1.96%	32.03%	B and D
% Segment profit to total profits	8.33%	66.67%	6.67%	18.33%	B and D
% Segment assets to total assets	31.25%	56.25%	5.00%	7.50%	A and B

Accordingly, A, B and D are reportable segments as per IFRS 8.

Further, since in the given case, external revenue of reportable segments is greater than 75% of entity's revenue (external), no additional operating segments should be identified as reportable segments.

4.7 (i) The manufacturing unit can be classified as held for sale due to the following reasons:

(a) The disposal group is available for immediate sale and in its present condition. The regulatory approval is customary and it is expected to be received in one year. The date at which the disposal group must be classified as held for sale is 31st July, 2021, i.e., the date at which management becomes committed to the plan.

(b) The sale is highly probable as the appropriate level of management i.e., board of directors in this case have approved the plan.

(c) A firm purchase agreement has been entered with the buyer.

(d) The sale is expected to be complete by 31st March, 2022, i.e., within one year from the date of classification.

(ii) Measurement of the manufacturing unit as on the date of classification as held for sale

Following steps need to be followed:

Step 1: Immediately before the initial classification of the asset (or disposal group) as held for sale, the carrying amounts of the asset (or all the assets and liabilities in the group) shall be measured in accordance with applicable IFRS. This has been done and the carrying value of the disposal group as on 31st July, 2021 is determined at ₹ 1,350. The difference between the carrying value as on 31st December, 2020 and 31st July, 2021 is accounted for as per the relevant IFRS.

Step 2: An entity shall measure a non-current asset (or disposal group) classified as held for sale at the lower of its carrying amount and fair value less costs to sell.

The fair value less cost to sell of the disposal group as on 31st July, 2021 is ₹ 875 (i.e.925-50). This is lower than the carrying value of ₹ 1,350. Thus, an impairment loss needs to be recognised and allocated first towards goodwill and thereafter pro-rata between non-current assets of the disposal group which are within the scope of IFRS 5 based on their carrying value.

Thus, the assets will be measured as under:

Particulars	**Carrying value – 31st July, 2021**	**Impairment**	**Carrying value as per IFRS 5 – 31st July, 2021**
Goodwill	300	(300)	-
Plant and Machinery	450	(57)	393
Building	925	(118)	807
Debtors	525	-	525
Inventory	200	-	200
Creditors	(125)	-	(125)
Loans	(925)	-	(925)
	1,350	(475)	875

4.8 Reconciliation of Plan assets and Defined benefit obligation:

	Defined benefit obligation ₹ in lakhs		Plan Assets ₹ in lakhs	
	31st Dec 2021	31st Dec 2020	31st Dec 2021	31st Dec 2020
Balance at the beginning of the year	63.25	47.08	21.80*	14.65
Current service cost	5.84	4.97	-	-
Interest cost	4.27	3.56	-	-
Changes in demographic assumptions	0.62	1.86	-	-
Changes in financial assumptions	3.58	1.93	-	-
Experience variance	(2.49)	4.46	-	-
Benefits paid	-	(0.61)	-	(0.61)
Investment income	-	-	1.47	1.12
Employers' contribution	-	-	8.00	7.00
Return on plan assets	-	-	2.12	(0.35)
Balance at the end of year	75.07	63.25	33.39	21.81*

In the Balance Sheet, the following will be recognised:

Net defined liability to be recognised for the period ending 31st December, 2020:

= ₹ 41.44 lakhs (₹ 63.25 lakhs - ₹ 21.81 lakhs)

Net defined liability to be recognised for the period ending 31st December, 2021:

= ₹ 41.68 lakhs (₹ 75.07 lakhs - ₹ 33.39 lakhs)

In the Statement of Profit and Loss, the following will be recognised:

	Defined benefit obligation ₹ in lakhs		Plan Assets ₹ in lakhs	
	31st Dec., 2021	31st Dec., 2020	31st Dec., 2021	31st Dec., 2020
Current service cost	5.84	4.97	-	-
Interest cost	4.27	3.56	-	-
Investment income	-	-	(1.47)	(1.12)
Total	10.11	8.53	(1.47)	(1.12)

Expense to be recognised in the Statement of Profit or Loss for the period ending 31st December, 2020 = ₹ 7.41 lakhs (₹ 8.53 lakhs - ₹ 1.12 lakhs)

Expense to be recognised in the Statement of Profit or Loss for the period ending 31st December, 2021 = ₹ 8.64 lakhs (₹ 10.11 lakhs - ₹ 1.47 lakhs)

Case Study Question 5

Nuogen Ltd. is a company which generates electricity and heat, and supplies electricity and natural gas. Nuogen Ltd. has diversified generating facilities, including renewable energy sources, natural gas and coal, pumped storage power stations and nuclear power stations.

On 1st April, 2019, Nuogen Ltd. had granted 1,20,000 share options to its employees with the vesting condition being a service condition as follows:

- *Vesting date : 31st March, 2020 - 80,000 share options (1-year vesting period since grant date)*
- *Vesting date : 31st March, 2023 - 40,000 share options (4-year vesting period since Grant date)*

Each option can be converted into one equity share of Nuogen Ltd. The fair value of the options on grant date, i.e., on 1st April, 2019 was ₹ 20.

However, the equity shares will be allotted to employees against the share options only after the employees complete 5 years of service from the initial grant date of the share options, i.e., on 31st March, 2024. Nuogen Ltd. is required to prepare financial statements in IFRS for the financial year ending 31st March, 2022. The transition date for IFRS being 1st April, 2020.

Nuogen Ltd. got loan from BOA Bank, 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. Nuogen Ltd. borrowed 10 lacs for a term of 5 years and 8 lacs for a term of 3 years.

Nuogen Ltd. had a machinery S with carrying amount of ₹ 10 lacs and a balance in revaluation reserve of ₹ 2.5 Lacs. The Company sold that machinery for 20 million.

Nuogen Ltd. also has an asset AS which cost ₹ 2,00,000. On 31st March, 2017, the carrying value was ₹ 1,80,000 and the asset was revalued to ₹ 2,20,000. No adjustment is made for tax purpose. Cumulative depreciation for tax purpose is ₹ 30,000 and rate is 30%.

Nuogen Ltd. has a nuclear power plant and a related decommissioning liability, The nuclear power plant started operating on 1st April, 2019. The plant has a useful life of 40 years. Its initial cost was ₹ 2,40,000. This included an amount for decommissioning costs of ₹ 20,000, *which represented ₹ 1,40,800 in estimated cash flows payable in 40 years discounted at a risk adjusted rate of 5 per cent. The entity's financial year ends on 31st March, 2022. A market-based discounted cash flow valuation of ₹ 2,30,000 is obtained at 31st March, 2022. This valuation is after deduction of an allowance of ₹ 23,200 for decommissioning costs, which represents no change to the original estimate, after the unwinding of three years' discount.*

On 31st March, 2023, the entity estimates that, as a result of technological advances, the present value of the decommissioning liability has decreased by ₹ 10,000. The entity decides that a full valuation of the asset is needed at 31st March, 2023, in order to ensure that the carrying amount does not differ materially from fair value. The asset is now valued at ₹ 2,14,000, which is net of an allowance for the reduced decommissioning obligation.

Nuogen Ltd. enters into a ten-year lease contract with a XYZ Ltd. to use an equipment. The contract includes maintenance services (as provided by lessor). XYZ Ltd. obtains its own insurance for the equipment. Annual payments are ₹ 10,000 (₹ 1,000 relate to maintenance services and ₹ 500 to insurance costs).

Nuogen Ltd. is able to determine that similar maintenance services and insurance costs are offered by third parties for ₹ 2,000 and ₹ 500 a year, respectively. Nuogen Ltd. is unable to find an observable stand-alone rental amount for a similar equipment because none leased without related maintenance services provided by the lessor.

Nuogen Ltd. also has taken on lease a factory building at a rental of ₹ 1,20,000 a year. There are 5 years remaining on the lease. The market rent is ₹ 50,000 a year. Nuogen Ltd. no longer occupies the factory building and it is not used in the business. A sublease (non-cancellable) on the factory building has been arranged at a rent of ₹ 50,000 a year for the remaining 5 years on the lease.

I. Multiple Choice Questions

5.1 On sale of machinery S, the balance amount in the revaluation reserve is

- *(A) Transferred to the asset account*
- *(B) Transferred directly to retained earnings*
- *(C) Transferred to profit and loss*
- *(D) Retained in revaluation reserve account itself.*

5.2 Inception of lease is

- *(A) Date of lease agreement.*
- *(B) Date of commitment by the parties to the principal provisions of the lease*
- *(C) (A) or (B), whichever is earlier.*
- *(D) Date of preparing the financial statement*

5.3 How much should be allocated as lease component for XYZ Ltd.?

(A) ₹ 10,000

(B) ₹ 9,500

(C) ₹ 8,000

(D) ₹ 7,500

5.4 Determine the provision amount that is to be provided for the factory building which is sub leased?

(A) ₹ 3,50,000

(B) ₹ 70,000

(C) ₹ 6,00,000

(D) ₹ 2,50,000

5.5 What are the deferred tax implications of the transaction in case of asset AS?

(A) Deferred tax asset of ₹ 15,000

(B) Deferred tax liability of ₹ 15,000

(C) No deferred tax implications

(D) Deferred tax asset of ₹ 20,000 ***(2 Marks each i.e. 2 x 5 = 10 Marks)***

II. Descriptive Questions

5.6 How the share-based payment should be reflected in the books of Nuogen Ltd. as on 31st March, 2022, assuming that no entry has been passed in the books of Nuogen Ltd. on grant date, i.e. 1st April, 2020?* ***(4 Marks)***

5.7 Compute the fair value upon initial recognition of the loan in the books of Nuogen Ltd. and how will loan processing fee be accounted? ***(3 Marks)***

5.8 How the entity will account for the changes in decommissioning liability if it adopts revaluation mode? ***(8 Marks)***

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* **PS:** Read 1st April, 2020 as 1st April, 2019.

Answer to Case Study 5

I. Answer to Multiple Choice Questions

5.1 Option (B) : Transferred directly to retained earnings

5.2 Option (C) : (A) or (B), whichever is earlier

5.3 Option (C) : ₹ 8,000

5.4 Option (A) : ₹ 3,50,000

5.5 Option (B) : Deferred tax liability of ₹ 15,000

II. Answer to Descriptive Questions

5.6 **<u>For 80,000 share-based options vested before transition date</u>**

IFRS 1 provides that a first-time adopter is encouraged, but not required, to apply IFRS 2 on 'Share-based Payment' to equity instruments that vested before the date of transition to IFRS. Hence, Nuogen Ltd. may opt for the exemption given in IFRS 1 for 80,000 share options vested before transition date. However, since no earlier accounting was done for this share-based options under previous GAAP too, therefore this led to error on the transition date detected on the reporting date i.e. 31st March, 2022. Hence, no exemption could be availed by Nuogen Ltd. on transition date w.r.t. IFRS 2.

It is assumed that the entity has disclosed publicly the fair value of those equity instruments, determined at the measurement date, as defined in IFRS 2. Further, it is also assumed that the previous applicable GAAP for the entity was IGAAP (AS) and therein, the entity had not adopted intrinsic method of valuation.

While preparing the financial statements for the financial year 2021-2022, an error has been discovered which occurred in the year 2019-2020, i.e., for the period which was earlier than earliest prior period presented; therefore, the error should be corrected by restating the opening balances of relevant assets and/or liabilities and relevant component of equity for the year 2020-2021.

Accordingly, on retrospective calculation of share based options w.r.t. 80,000 options, Nuogen Ltd. will create 'Share based payment reserve (equity)' with ₹ 16,00,000 and correspondingly adjust the same though retained earnings.

<u>For 40,000 share-based options to be vested on 31st March, 2023</u>

Since share-based options have not been vested before transition date, no option as per IFRS 1 is available to Nuogen Ltd. The entity will apply IFRS 2 retrospectively. However, Nuogen Ltd. did not account for the same at the grant date. Therefore, while preparing the financial statements for the financial year 2021-2022, an error has been discovered which occurred in the year 2019-2020, i.e., for the period which was earlier than earliest prior period presented; therefore, the error should be corrected by restating the opening balances of relevant assets and/or liabilities and relevant component of equity for the year 2020-2021. This will result in consequential restatement of balances as at 1st April, 2020 (i.e, opening balance sheet as on 1st April, 2020). Adjustment is to be made by recognising the 'Share based payment reserve (equity)' and adjusting the retained earnings by ₹ 2,00,000.

Further, expenses for the year ended 31st March, 2021 and share based payment reserve (equity) as at 31st March, 2021 were understated because of non-recognition of 'employee benefits expense' and related reserve. To correct the above errors in the annual financial statements for the year ended 31st March, 2022, the entity should restate the comparative amounts (i.e., those for the year ended 31st March, 2021) in the statement of profit and loss. In the given case, 'Share based payment reserve (equity)' would be credited by ₹ 2,00,000 and 'employee benefits expense' would be debited by ₹ 2,00,000

For the year ending 31st March, 2022, 'Share based payment reserve (equity)' would be credited by ₹ 2,00,000 and 'employee benefits expense' would be debited by ₹ 2,00,000.

Working Note:

Period	Lot	Proportion	Fair value	Cumulative expenses	Expenses
		a	b	d= b x a	e = d-pvs period d
2019-2020	1 (1-year vesting period)	1/1	16,00,000	16,00,000	16,00,000
2019-2020	2 (4-year vesting period)	1/4	8,00,000	2,00,000	2,00,000
2020-2021	2 (4-year vesting period)	2/4	8,00,000	4,00,000	2,00,000
2021-2022	2 (4-year vesting period)	3/4	8,00,000	6,00,000	2,00,000

5.7 The loan taken by Nuogen Ltd. shall be measured upon initial recognition as follows:

At transaction price less processing fee ie.:

For Loan of ₹ 10 lacs = ₹ 9,90,000 (10,00,000 – 10,000) will be recognised as the fair value of the loan on the initial date

For Loan of ₹ 8 lacs = ₹ 7,92,000 (8,00,000 – 8,000) will be recognised as the fair value of the loan on the initial date

Hence, the fair value of both the loans is ₹ 17,82,000 (₹ 9,90,000 + ₹ 7,92,000).

In case of financial liability, loan processing fee of ₹ 18,000 (10,000 + 8,000) [Transaction costs] is included in calculation of effective interest rate (EIR) and amortised over expected life of the instrument. In other words, in subsequent measurement, Interest is to be accrued using effective rate of interest over the period of loan.

Due to charging of loan processing fee by the bank, finance cost to be record in the books for both the loans will not be the interest charged by the bank rather it would be computed and charged as per EIR (to be computed by Nuogen Ltd.)

Balances at 31st March, 2022:	**₹**
Asset at valuation (1)	2,53,200
Accumulated depreciation	Nil
Decommissioning liability	(23,200)
Net assets	2,30,000
Retained earnings (2)	(21,200)
Revaluation surplus (3)	31,200

Notes:

(1) When accounting for revalued assets to which decommissioning liabilities attach, it is important to understand the basis of the valuation obtained. For example:

(a) if an asset is valued on a discounted cash flow basis, some valuers may value the asset without deducting any allowance for decommissioning costs (a 'gross' valuation), whereas others may value the asset after deducting an allowance for decommissioning costs (a 'net' valuation), because an entity acquiring the asset will generally also assume the decommissioning obligation. For financial reporting purposes, the decommissioning obligation is recognised as a separate liability, and is not deducted from the asset. Accordingly, if the asset is valued on a net basis, it is necessary to adjust the valuation obtained by adding back the allowance for the liability, so that the liability is not counted twice.

(b) if an asset is valued on a depreciated replacement cost basis, the valuation obtained may not include an amount for the decommissioning component of the asset. If it does not, an appropriate amount will need to be added to the valuation to reflect the depreciated replacement cost of that component.

Since, the asset is valued on a net basis, it is necessary to adjust the valuation obtained by adding back the allowance for the liability. Valuation obtained of ₹ 2,30,000 plus decommissioning costs of ₹ 23,200, allowed for in the valuation but recognised as a separate liability = ₹ 2,53,200.

(2) Three years' depreciation on original cost ₹ 2,40,000 x 3/40 = ₹ 18,000 plus cumulative discount on ₹ 20,000 at 5 per cent compound = ₹ 3,200 (23,200 - 20,000);

Total = ₹ 18,000 + ₹ 3,200 = ₹ 21,200.

(3) Revalued amount ₹ 2,53,200 less previous net book value of ₹ 2,22,000 (cost ₹ 2,40,000 less accumulated depreciation ₹ 18,000) i.e. ₹ 2,53,200 – ₹ 2,22,000 = ₹ 31,200.

The depreciation expense for 2022-2023 is therefore ₹ 6,843 (₹ 2,53,200 x 1 / 37) and the discount expense for 2022-2023 is ₹ 1,160. On 31st March, 2023, the decommissioning liability (before any adjustment) is ₹ 24,360. However, as per estimate of the entity, the present value of the decommissioning liability has decreased by ₹ 10,000. Accordingly, the entity adjusts the decommissioning liability from ₹ 24,360 to ₹ 14,360.

The whole of this adjustment is taken to revaluation surplus, because it does not exceed the carrying amount that would have been recognised had the asset been carried under the cost model. If it had done, the excess would have been taken to profit or loss.

The entity makes the following journal entry to reflect the change:

		₹	₹
Provision for decommissioning liability	Dr.	10,000	
To Revaluation surplus			10,000

As at 31st March, 2023, the entity revalued its asset at ₹ 2,14,000, which is net of an allowance of ₹ 14,360 for the reduced decommissioning obligation that should be recognised as a separate liability. The valuation of the asset for financial reporting purposes, before deducting this allowance, is therefore ₹ 2,28,360.

The following additional journal entry is needed:

Notes:

		₹	₹
Accumulated depreciation (1)	Dr.	6,843	
To Asset at valuation			6,843
Revaluation surplus (2)	Dr.	17,997	
To Asset at valuation (3) (2,53,200–6,843–2,28,360)			17,997

(1) Eliminating accumulated depreciation of ₹ 6,843 in accordance with the entity's accounting policy.

(2) The debit is to revaluation surplus because the deficit (₹ 17,997) arising on the revaluation does not exceed the credit balance (₹ 31,200) existing in the revaluation surplus in respect of the asset.

(3) Previous valuation (before allowance for decommissioning costs) ₹ 2,53,200, less cumulative depreciation ₹ 6,843, less new valuation (before allowance for decommissioning costs) ₹ 2,28,360.

Following this valuation, the amounts included in the balance sheet of 31st March, 2023 are:

	₹
Asset at valuation	2,28,360
Accumulated depreciation	Nil
Decommissioning liability	(14,360)
Net assets	2,14,000
Retained earnings (1)	(29,203)
Revaluation surplus (2) (31,200 + 10,000 – 17,997)	23,203

Notes:

(1) ₹ 21,200 at 31st March, 2022, plus depreciation expense of ₹ 6,843 and discount expense of ₹ 1,160 = ₹ 29,203.

(2) ₹ 31,200 at 31st March, 2022, plus ₹ 10,000 arising on the decrease in the liability, less ₹ 17,997 deficit on revaluation = ₹ 23,203.