Test Series: October, 2019

MOCK TEST PAPER

FINAL (NEW) COURSE: GROUP – I

PAPER – 1: FINANCIAL REPORTING

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

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

Working notes should form part of the answers.

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

1. (a) H Ltd. has the following assets and liabilities as at March 31, 20X1, prepared in accordance with previous GAAP:

Particulars	Notes	Amount (Rs.)
Property, Plant and Equipment	1	1,34,50,000
Investments in S. Ltd.	2	48,00,000
Debtors		2,00,000
Advances for purchase of inventory		50,00,000
Inventory		8,00,000
Cash		49,000
Total assets		2,42,99,000
Deferral loan	3	60,00,000
Creditors		30,00,000
Short term borrowing		8,00,000
Provisions		12,00,000
Total liabilities		1,10,00,000
Share capital		1,30,00,000
Reserves:		2,99,000
Cumulative translation difference	4	1,00,000
ESOP reserve	4	20,000
Retained earnings		1,79,000
Total equity		1,32,99,000
Total equity and liabilities		2,42,99,000

The following GAAP differences were identified by the Company on first-time adoption of Ind AS with effect from April 1, 20X1:

1. In relation to property, plant and equipment, the following adjustments were identified:
   - Property, plant and equipment comprise land held for capital appreciation purposes costing Rs. 4,50,000 and was classified as investment property as per Ind AS 40.
   - Exchange differences of Rs. 1,00,000 were capitalised to depreciable property, plant and equipment on which accumulated depreciation of Rs. 40,000 was recognised.
   - There were no asset retirement obligations.
   - The management intends to adopt deemed cost exemption for using the previous GAAP carrying values as deemed cost as at the date of transition for PPE and investment property.
2. The Company had made an investment in S Ltd. (subsidiary of H Ltd.) for Rs. 48,00,000 that carried a fair value of Rs. 68,00,000 as at the transition date. The Company intends to recognise the investment at its fair value as at the date of transition.
3. Financial instruments:
   - **Deferral loan Rs. 60,00,000:**

   The deferral loan of Rs. 60,00,000 was obtained on March 31, 20X1, for setting up a business in a backward region with a condition to create certain defined targets for employment of local population of that region. The loan does not carry any interest and is repayable in full at the end of 5 years. In accordance with Ind AS 109, the discount factor on the loan is to be taken as 10%, being the incremental borrowing rate. Accordingly, the fair value of the loan as at March 31, 20X1, is Rs. 37,25,528. The entity chooses to exercise the option given in paragraph B11 of Ind AS 101, i.e., the entity chooses to apply the requirements of Ind AS 109, Financial Instruments and Ind AS 20, Accounting for Government Grants and Disclosure of Government Assistance, retrospectively as required information had been obtained at the time of initially accounting for deferral loan.
4. The retained earnings of the Company contained the following:
   - **ESOP reserve of Rs. 20,000:**

   The Company had granted 1,000 options to employees out of which 800 have already vested. The Company followed an intrinsic value method for recognition of ESOP charge and recognised Rs. 12,000 towards the vested options and Rs. 8,000 over a period of time as ESOP charge and a corresponding reserve. If fair value method had been followed in accordance with Ind AS 102, the corresponding charge would have been Rs. 15,000 and Rs. 9,000 for the vested and unvested shares respectively. The Company intends to avail the Ind AS 101 exemption for share-based payments for not restating the ESOP charge as per previous GAAP for vested options.

- **Cumulative translation difference :**

  Rs. 1,00,000 The Company had a non-integral foreign branch in accordance with AS 11 and had recognised a balance of Rs. 1,00,000 as part of reserves. On first-time adoption of Ind AS, the Company intends to avail Ind AS 101 exemption of resetting the cumulative translation difference to zero. **(15 Marks)**

(b) Sumeru Limited holds 35% of total equity shares of Meru Limited, an associate company. The value of Investments in Meru Limited on March 31, 20X1 is Rs. 3 crores in the consolidated financial statements of Sumeru Limited.

Sumeru Limited sold goods worth Rs. 3,50,000 to Meru Limited. The cost of goods sold. is Rs. 3,00,000. Out of these, goods costing Rs. 1,00,000 to Meru Limited were in the closing stock of Meru Limited.

During the year ended March 31, 20X2 the profit and loss statement of Meru Limited showed a loss of Rs. 1 crore.

(A) What is the value of investment in Meru Limited as on March 31, 20X2 in the consolidated financial statements of Sumeru Limited, if equity method is adopted for valuing the investments in associates?

(B) Will your answer be different if Meru Limited had earned a profit of Rs. 1.50 crores and declared a dividend of Rs. 75 lacs to the equity shareholders of the Company?

(5 Marks)

2. (a) RKA Private Ltd is an old company established in 1995. The company started with a very small capital base and today it is one of the leading companies in India in its industry. The company has an annual turnover of Rs. 11,000 crores and planning to get listed in the next year.

The company has a large employee base. The company provided a defined benefit plan to its employees. Following is the information relating to the balances of the fund's assets and liabilities as at 1st April, 20X1 and 31st March, 20X2. Rs. in lacs

Particulars	1st April, 20X1	31st March, 20X2
Present value of benefit obligation	1,400	1,580
Fair value of plan assets	1,140	1,275

For the financial year ended 31st March, 20X2, service cost was Rs. 55 lacs. The company made a contribution of an amount of Rs. 111 lacs to the plan. No benefits were paid during the year.

Consider a discount rate of 8%.

As per Ind AS, you are required to -

(a) Compute the balance(s) of the company to be included its balance sheet as on 31st March, 20X2 and amounts to be recognized in the statement of profit and loss and other comprehensive income for the year ended 31st March, 20X2.

(b) Give the journal entries in respect of amount(s) to be recognized. **(8 Marks)**

(b) How should contingent consideration payable in relation to a business combination be accounted for on initial recognition and at the subsequent measurement as per Ind AS in the following cases:

i) On 1 April 20X1, A Ltd. acquires 100% interest in B Ltd. As per the terms of agreement the purchase consideration is payable in the following 2 tranches:

- ❖ an immediate issuance of 10 lakhs shares of A Ltd. having face value of Rs. 10 per share;
- ❖ a further issuance of 2 lakhs shares after one year if the profit before interest and tax of B Ltd. for the first year following acquisition exceeds Rs. 1 crore.

The fair value of the shares of A Ltd. on the date of acquisition is Rs. 20 per share. Further, the management has estimated that on the date of acquisition, the fair value of contingent consideration is Rs. 25 lakhs.

During the year ended 31 March 20X2, the profit before interest and tax of B Ltd. exceeded Rs. 1 crore. As on 31 March 20X2, the fair value of shares of A Ltd. is Rs. 25 per share.

ii) Continuing with the fact pattern in (a) above except for:

- ❖ The number of shares to be issued after one year is not fixed.
- ❖ Rather, A Ltd. agreed to issue variable number of shares having a fair value equal to Rs. 40 lakhs after one year, if the profit before interest and tax for the first year following acquisition exceeds Rs. 1 crore. A Ltd. issued shares with Rs. 40 lakhs after an year. **(12 Marks)**

3. (a) X Ltd. has identified 4 operating segments for which revenue data is given below:

	External Sale (Rs.)	**Internal Sale (Rs.)**	**Total (Rs.)**
Segment A	30,00,000	Nil	30,00,000
Segment B	6,50,000	Nil	6,50,000
Segment C	8,50,000	1,00,000	9,50,000
Segment D	5,00,000	49,00,000	54,00,000
Total Sales	**50,00,000**	**50,00,000**	**1,00,00,000**

Additional information:

Segment C is a new business unit and management expect this segment to make a significant contribution to external revenue in coming years.

Which of the segments would be reportable under the criteria identified in Ind AS 108?

(5 Marks)

(b) X Ltd. sold JCB Machine having WDV of Rs. 50 Lakhs to Y Ltd. for Rs. 60 Lakhs and the same JCB was leased back by Y Ltd. to X Ltd. The lease is operating lease. Comment according to relevant Ind AS if:

(a) Sale price of Rs. 60 Lakhs is equal to fair value.

(b) Fair value is Rs. 50 Lakhs and sale price is Rs. 45 Lakhs.

(c) Fair value is Rs. 55 Lakhs and sale price Rs. 62 Lakhs.

(d) Fair value is Rs. 45 Lakhs and sale price is Rs. 48 Lakhs. **(5 Marks)**

(c) Tee Limited is carrying on the business of developing light weight and medium weight guns for the Indian defence industry. Tee Limited acquired 48% of shares in Kay Limited, a company engaged in advanced research in weapons. Tee Limited acquired shares in Kay Limited to substantiate their position in the industry.

The remaining 52% of shares are held by the key management personnel of the Company Kay Limited. The Kay management consists of eleven people who are experts in the fields of advanced weapons and the core of the Company.

Tee Limited has the option to purchase remaining 52% at any time by paying 6 times the market price of the share. But on purchase of the shares it is highly possible that the key management personnel will leave the company.

(A) State whether Tee Limited has control over Kay Limited.

(B) What will be your answer if Tee Limited had 51% of shares in Kay Limited and Kay Limited can start the research, development and production of weapon only with the stringent approval process of the defence ministry of the Central Government.

(5 Marks)

(d) Mittal Motors Limited is preparing financials for the year ended March 31, 20X2. The Company had some queries in preparation of certain data that is required to be presented in the financials. As the retainer of the Company, please advise the company for the following issues:

(i) Mittal Motors has issued 10,00,000 numbers of 9% cumulative preference shares. The Company has arrears of Rs. 15 crores of preference dividend as on March 31, 20X2, it includes current year arrears of Rs. 1.75 crores. The Company did not declare any dividend for equity shareholders as well as for preference shareholders.

What is the amount of dividend to be reduced from profit or loss for the year for calculating basic Earnings Per Share?

(ii) Further Mittal Motors has also issued certain convertible debentures, which are outstanding as at the year end. For the purpose of computation of weighted average number of shares (to arrive at diluted EPS) when should the dilutive potential shares should be deemed to have been converted into shares?

(A) At the start of the period.

(B) The date of issue of the potential shares

(C) At the start of the period or, if later, the date of the issue of the potential shares

(D) At the end of the period. **(5 Marks)**

4. (a) KK Ltd. runs a departmental store which awards 10 points for every purchase of Rs. 500 which can be discounted by the customers for further shopping with the same merchant. Unutilised points will lapse on expiry of two years from the date of credit. Value of each point is Rs. 0.50. During the accounting period 20X1-20X2, the entity awarded 1,00,00,000 points to various customers of which 18,00,000 points remained undiscounted. The management expects only 80% will be discounted in future of which normally 60-70% are redeemed during the next year.

The Company has approached your firm with the following queries and has asked you to suggest the accounting treatment (Journal Entries) under the applicable Ind AS for these award points:

(a)	How should the recognition be done for the sale of goods worth Rs. 10,00,000 on a particular day?
(b)	How should the redemption transaction be recorded in the year 20X1-20X2? The Company has requested you to present the sale of goods and redemption as independent transaction. Total sales of the entity is Rs. 5,000 lakhs.
(c)	How much of the deferred revenue should be recognised at the year-end (20X1-20X2) because of the estimation that only 80% of the outstanding points will be redeemed?
(d)	In the next year 20X2-20X3, 60% of the outstanding points were discounted Balance 40% of the outstanding points of 20X1-20X2 still remained outstanding. How much of the deferred revenue should the merchant recognize in the year 20X2-20X3 and what will be the amount of balance deferred revenue?
(e)	How much revenue will the merchant recognized in the year 20X2-20X3, if 3,00,000 points are redeemed in the year 20X2-20X3?

(14 Marks)

(b) A Ltd., whose functional currency is Indian Rupee, had a balance of cash and cash equivalents of Rs. 2,00,000, but there are no trade receivables or trade payables balances as on 1st April, 20X1. During the year 20X1-20X2, the entity entered into the following foreign currency transactions:

- ❖ A Ltd. purchased goods for resale from Europe for €2,00,000 when the exchange rate was €1 = Rs. 50. This balance is still unpaid at 31st March, 20X2 when the exchange rate is €1 = Rs. 45. An exchange gain on retranslation of the trade payable of Rs. 5,00,000 is recorded in profit or loss.
- ❖ A Ltd. sold the goods to an American client for $ 1,50,000 when the exchange rate was $1 = Rs. 40. This amount was settled when the exchange rate was $1 = Rs. 42. A further exchange gain regarding the trade receivable is recorded in the statement of profit or loss.
- ❖ A Ltd. also borrowed €1,00,000 under a long-term loan agreement when the exchange rate was €1 = Rs. 50 and immediately converted it to Rs. 50,00,000. The loan was retranslated at 31st March, 20X2 @ Rs. 45, with a further exchange gain recorded in the statement of profit or loss.
- ❖ A Ltd. therefore records a cumulative exchange gain of Rs. 18,00,000 (10,00,000 + 3,00,000 + 5,00,000) in arriving at its profit for the year.
- ❖ In addition, A Ltd. records a gross profit of Rs. 10,00,000 (Rs. 60,00,000 – Rs. 50,00,000) on the sale of the goods.
- ❖ Ignore taxation.

How cash flows arising from the above transactions would be reported in the statement of cash flows of A Ltd. under indirect method? **(6 Marks)**

5. (a) ABC Company issued 10,000 compulsory cumulative convertible preference shares (CCCPS) as on 1 April 20X1 @ Rs 150 each. The rate of dividend is 10% payable every year. The preference shares are convertible into 5,000 equity shares of the company at the end of 5th year from the date of allotment. When the CCCPS are issued, the prevailing market interest rate for similar debt without conversion options is 15% per annum. Transaction cost on the date of issuance is 2% of the value of the proceeds.

Key terms:

Date of Allotment	01-Apr-20X1
Date of Conversion	01-Apr-20X6
Number of Preference Shares	10,000
Face Value of Preference Shares	150
Total Proceeds	15,00,000

Rate of dividend	10%
Market Rate for Similar Instrument	15%
Transaction Cost	30,000
Face value of equity share after conversion	10
Number of equity shares to be issued	5,000
Effective interest rate	15.86%

You are required to compute the liability and equity component and pass journal entries for entire term of arrangement i.e. from the issue of preference shares till their conversion into equity shares keeping in view the provisions of relevant Ind AS. **(12 Marks)**

(b) An entity has a nuclear power plant and a related decommissioning liability. The nuclear power plant started operating on 1st April, 20X1. The plant has a useful life of 40 years. Its initial cost was ₹ 1,20,000. This included an amount for decommissioning costs of ₹ 10,000, which represented ₹ 70,400 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. Assume that a market-based discounted cash flow valuation of ₹ 1,15,000 is obtained at 31st March, 20X4. This valuation is after deduction of an allowance of ₹ 11,600 for decommissioning costs, which represents no change to the original estimate, after the unwinding of three years' discount. On 31st March, 20X5, the entity estimates that, as a result of technological advances, the present value of the decommissioning liability has decreased by ₹ 5,000. The entity decides that a full valuation of the asset is needed at 31st March, 20X5, in order to ensure that the carrying amount does not differ materially from fair value. The asset is now valued at ₹ 1,07,000, which is net of an allowance for the reduced decommissioning obligation.

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

6. (a) A Ltd. intends to open a new retail store in a new location in the next few weeks. It has spent a substantial sum on a series of television advertisements to promote this new store. It has paid for advertisements costing Rs. 8,00,000 before 31st March, 20X2. Rs. 7,00,000 of this sum relates to advertisements shown before 31st March, 20X2 and Rs. 1,00,000 to advertisements shown in April, 20X2. Since 31st March, 20X2, A Ltd. has paid for further advertisements costing Rs. 4,00,000. The accountant charged all these costs as expenses in the year to 31 March 20X2. However, CFO of A Ltd. does not want to charge Rs.12,00,000 against my 20X1-20X2 profits. He believes that these costs can be carried forward as intangible assets because the company's market research indicates that this new store is likely to be highly successful.

OR

As at 31st March, 20X1, a plantation consists of 100 Pinus Radiata trees that were planted 10 years earlier. The tree takes 30 years to mature, and will ultimately be processed into building material for houses or furniture. The enterprise's weighted average cost of capital is 6% p.a.

Only mature trees have established fair values by reference to a quoted price in an active market. The fair value (inclusive of current transport costs to get 100 logs to market) for a mature tree of the same grade as in the plantation is:

As at 31st March, 20X1: 171

As at 31st March, 20X2: 165

Assume that there would be immaterial cash flow between now and point of harvest.

The present value factor of Rs. 1 @ 6% for

19^{th} year = 0.331

20^{th} year = 0.312

State the value of such plantation as on 31st March, 20X1 and 20X2 and the gain or loss to be recognised as per Ind AS. **(6 Marks)**

(b) ABC Ltd. is a company which has a net worth of Rs. 200 crores, it manufactures rubber parts for automobiles. The sales of the company are affected due to low demand of its products.

The previous year's financials state: (Rs. in Crores)

	March 31, 20X4 (Current year)	March 31, 20X3	March 31, 20X2	March 31, 20X1
Net Profit	3.00	8.50	4.00	3.00
Sales (turnover)	850	950	900	800

Required

Does the Company have an obligation to form a CSR committee since the applicability criteria is not satisfied in the current financial year? **(6 Marks)**

(c) Croton Limited is engaged in the business of trading commodities. The company's main asset are investments in equity shares, preference shares, bonds, non-convertible debenture (NCD) and mutual funds.

The Company collects the periodical income (i.e. interest, dividend, etc.) from the investments and regularly sells the investment in case of favouable market conditions. Such investments have been classified as non-current investments in the financial statements.

Also, the company buys and sells equity shares of companies for earning short term profits from the stock market.

The CFO of company classified all the non-current investments as Fair Value Through Other Comprehensive Income (FVTOCI) and all the current investment as Fair value Through Profit and Loss (FVTPL).

Croton Limited raised the following queries:

(a) Can the Company classify the equity shares previously held under current investment as FVTOCI if the company decides to hold them for more than one-year (i.e. classify it as non-current)?

(b) The Company had classified NCDs with a maturity period of less than twelve months from the reporting period as current. This has been classified as FVTPL by the CFO of the company. The Company wants to know whether these NCDs can be recognized as FVTOCI? **(8 Marks)**