Test Series: October, 2020

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) Summarized Balance Sheets of PN Ltd. and SR Ltd. as on 31 March 2020 were given as below:

(Amount in ₹)

Particulars	PN Ltd.	SR Ltd.
Assets		
Land & building	4,68,000	5,61,600
Plant & Machinery	7,48,800	4,21,200
Investment in SR Ltd.	12,48,000	-
Inventories	3,74,400	1,13,600
Trade Receivables	1,86,500	1,24,800
Cash & Cash equivalents	45,200	24,900
Total Assets	**30,70,900**	**12,46,100**
Equity & Liabilities		
Equity Share Capital (Shares of ₹ 100 each fully paid)	15,60,000	6,24,000
Other Reserves	9,36,000	3,12,000
Retained Earnings	1,78,400	2,55,800
Trade Payables	1,46,900	34,300
Short-term borrowings	2,49,600	20,000
Total Equity & Liabilities	**30,70,900**	**12,46,100**

(i) PN Ltd. acquired 70% equity shares of ₹ 100 each of SR Ltd. on 1 October 2019.

(ii) The Retained Earnings of SR Ltd. showed a credit balance of ₹ 93,600 on 1 April 2019 out of which a dividend of 12% was paid on 15 December 2019.

(iii) PN Ltd. has credited the dividend received to its Retained Earnings.

(iv) Fair value of Plant & Machinery of SR Ltd. as on 1 October 2019 was ₹ 6,24,000. The rate of depreciation on Plant & Machinery was 10% p.a.

(v) Following are the increases on comparison of Fair Value as per respective Ind AS with book value as on 1 October 2019 of SR Ltd. which are to be considered while consolidating the Balance Sheets:

(a) Land & Buildings ₹ 3,12,000

(b) Inventories ₹ 46,800

(c) Trade Payables ₹ 31,200.

(vi) The inventory is still unsold on Balance Sheet date and the Trade Payables are not yet settled.

(vii) Other Reserves as on 31 March 2020 are the same as was on 1 April 2019.

(viii) The business activities of both the company are not seasonal in nature and therefore, it can be assumed that profits are earned evenly throughout the year.

Prepare the Consolidated Balance Sheet as on 31 March 2020 of the group of entities PN Ltd. and SR Ltd. **(16 Marks)**

(b) CARP Ltd. is engaged in developing computer software. The expenditures incurred by CARP Ltd. in pursuance of its development of software is given below:

(i) Paid ₹ 1,50,000 towards salaries of the program designers.

(ii) Incurred ₹ 3,00,000 towards other cost of completion of program design.

(iii) Incurred ₹ 80,000 towards cost of coding and establishing technical feasibility.

(iv) Paid ₹ 3,00,000 for other direct cost after establishment of technical feasibility.

(v) Incurred ₹ 90,000 towards other testing costs.

(vi) A focus group of other software developers was invited to a conference for the introduction of this new software. Cost of the conference aggregated to ₹ 60,000.

(vii) On 15 March 2020, the development phase was completed and a cash flow budget was prepared.

Net profit for the year 2019-2020 was estimated to be equal to ₹ 30,00,000.

How CARP Ltd. should account for the above-mentioned cost as per relevant Ind AS?

(4 Marks)

2. (a) PQR Ltd. is the company which has performed well in the past but one of its major assets, an item of equipment, suffered a significant and unexpected deterioration in performance. Management expects to use the machine for a further four years after 31 March 2020, but at a reduced level. The equipment will be scrapped after four years. The financial accountant for PQR Ltd. has produced a set of cash-flow projections for the equipment for the next four years, ranging from optimistic to pessimistic. CFO thought that the projections were too conservative, and he intended to use the highest figures each year. These were as follows:

	₹
Year ended 31 March 2021	2,76,000
Year ended 31 March 2022	1,92,000
Year ended 31 March 2023	1,20,000
Year ended 31 March 2024	1,14,000

The above cash inflows should be assumed to occur on the last day of each financial year. The pre-tax discount rate is 9%. The machine could have been sold at 31 March 2020 for ₹ 6,00,000 and related selling expenses in this regard could have been ₹ 96,000. The machine was revalued previously, and at 31 March 2020 an amount of ₹ 36,000 was held in revaluation surplus in respect of the asset. The carrying value of the asset at 31 March 2020 was ₹ 6,60,000. The Indian government has indicated that it may compensate the company for any loss in value of the assets up to its recoverable amount. **(5 Marks)**

(b) On 1 April 2019, the fair value of the assets of XYZ Ltd.'s defined benefit plan were valued at ₹ 20,40,000 and the present value of the defined obligation was ₹ 21,25,000. On 31 March 2020 the plan received contributions from XYZ Ltd. amounting to ₹ 4,25,000 and paid out benefits of ₹ 2,55,000. The current service cost for the financial year ending 31 March 2020 is ₹ 5,10,000. An interest rate of 5% is to be applied to the plan assets and obligations. The fair value of the plan's assets at 31 March 2020 was ₹ 23,80,000, and the present value of the defined benefit obligation was ₹ 27,20,000. Provide a reconciliation from the opening balance to the closing balance for Plan assets and Defined benefit obligation. Also show how much amount should be recognised in the statement of profit and loss, other comprehensive income and balance sheet? **(5 Marks)**

(c) On 1 April 2019, Shelter Ltd. issued 5,000, 8% debentures maturing on 31 March 2024. The debentures are convertible at the option of the holder into equity shares of Shelter Ltd. at a conversion price of ₹ 105 per share or redeemable at face value of Rs. 100 each. Interest is payable annually in cash. At the date of issue, Shelter Ltd. could have issued non-convertible debt with a 5 year term bearing a coupon interest rate of 12%. On 1 April 2022, the convertible debentures have a fair value of ₹ 5,25,000. Shelter Ltd. makes a tender offer to debenture holders to repurchase the debentures for ₹ 5,25,000, which the holders accepted. At the date of repurchase, Shelter Ltd. could have issued non-convertible debt with a 2 year term bearing a coupon interest rate of 9%.

Show accounting entries in the books of Shelter Ltd. for recording of equity and liability component:

(i) At the time of initial recognition and

(ii) At the time of repurchase of the convertible debentures.

The following present values of ₹ 1 at 8%, 9% & 12% are supplied to you:

Interest Rate	Year 1	Year 2	Year 3	Year 4	Year 5
8%	0.926	0.857	0.794	0.735	0.681
9%	0.917	0.842	0.772	0.708	0.650
12%	0.893	0.797	0.712	0.636	0.567

(10 Marks)

3. (a) Deepak Ltd., an automobile group acquires 25% of the voting ordinary shares of Shaun Ltd., another automobile business, by paying, ₹ 4,320 crore on 01.04.2019. Deepak Ltd. accounts its investment in Shaun Ltd. using equity method as prescribed under Ind AS 28. At 31.03.2020, Deepak Ltd. recognised its share of the net asset changes of Shaun Ltd. using equity accounting as follows:

	(₹ in crore)
Share of Profit or Loss	378
Share of Exchange difference in OCI	54
Share of Revaluation Reserve of PPE in OCI	27

On 01.04.2020, Deepak Ltd. acquired remaining 75% of Shaun Ltd. for cash ₹ 13,500 crore. Fair value of the 25% interest already owned was ₹ 4,860 crore and fair value of Shaun Ltd.'s identifiable net assets was ₹ 16,200 crore as on 01.04.2020.

How should such business combination be accounted for in accordance with the applicable Ind AS? **(8 Marks)**

(b) An entity engaged in automobile sector has assessed the impact of COVID-19 outbreak on its future viability of business model. Senior Management has identified the need for restructuring some of its business activities and retrenching its employees in many areas. Senior Management is drawing up a plan for the consideration of the Board of Directors in their meeting scheduled in May 2020, which is subsequent to the reporting date of the current financial year i.e. 31 March 2020. Can the entity recognise provisions for restructuring costs in the financial statements of the current year i.e. 2019-2020? **(4 Marks)**

(c) KK Ltd. has granted an interest free loan of ₹ 10,00,000 to its wholly owned Indian Subsidiary YK Ltd. There is no transaction cost attached to the said loan. The Company has not finalised any terms and conditions including the applicable interest rates on such loans. The Board of Directors of the Company are evaluating various options and has requested your firm to provide your views under Ind AS in following situations:

(i) The Loan given by KK Ltd. to its wholly owned subsidiary YK Ltd. is interest free and such loan is repayable on demand.

(ii) The said Loan is interest free and will be repayable after 3 years from the date of granting such loan. The current market rate of interest for similar loan is 10%. Considering the same, the fair value of the loan at initial recognition is ₹8,10,150.

(iii) The said loan is interest free and will be repaid as and when YK Ltd. has funds to repay the Loan amount.

Based on the same, KK Ltd. has requested you to suggest the accounting treatment of the above loan in the stand-alone financial statements of KK Ltd. and YK Ltd. and also in the consolidated financial statements of the group. Consider interest for only one year on the above loan for the purpose of providing journal entries. **(8 Marks)**

4. Shaurya Limited is the company having its registered and corporate office at New Delhi. 60% of the Shaurya Limited's shares are held by the Government of India and rest by other investors.

This is the first time that Shaurya limited would be applying Ind AS for the preparation of its financials for the current financial year 2019-2020. Following balance sheet is prepared as per earlier GAAP as at the beginning of the preceding period along with the additional information:

Balance Sheet as at 31 March 2018

(All figures are in '000, unless otherwise specified)

Particulars	Amount
EQUITY AND LIABILITIES	
(1) Shareholders' Funds	
(a) Share Capital	10,00,000
(b) Reserves & Surplus	25,00,000
(2) Non-Current Liabilities	
(a) Long Term Borrowings	4,50,000
(b) Long Term Provisions	3,50,000
(c) Deferred tax liabilities	3,50,000
(3) Current Liabilities	
(a) Trade Payables	22,00,000
(b) Other Current Liabilities	4,50,000
(c) Short Term Provisions	12,00,000
TOTAL	85,00,000

ASSETS	
(1) Non-Current Assets	
(a) Property, Plant & Equipment (net)	20,00,000
(b) Intangible assets	2,00,000
(c) Goodwill	1,00,000
(d) Non-current Investments	5,00,000
(e) Long Term Loans and Advances	1,50,000
(f) Other Non-Current Assets	2,00,000
(2) Current Assets	
(a) Current Investments	18,00,000
(b) Inventories	12,50,000
(c) Trade Receivables	9,00,000
(d) Cash and Bank Balances	10,00,000
(e) Other Current Assets	4,00,000
TOTAL	85,00,000

Additional Information (All figures are in '000) :

1. Other current liabilities include ₹ 3,90,000 liabilities to be paid in cash such as expense payable, salary payable etc. and ₹ 60,000 are statutory government dues.
2. Long term loans and advances include ₹ 40,000 loan and the remaining amount consists Advance to staff of ₹ 1,10,000.
3. Other non-current assets of ₹ 2,00,000 consists Capital advances to suppliers.
4. Other current assets include ₹ 3,50,000 current assets receivable in cash and Prepaid expenses of ₹ 50,000.
5. Short term provisions include Dividend payable of ₹ 2,00,000. The dividend payable had been as a result of board meeting wherein the declaration of dividend for financial year 2017-2018 was made. However, it is subject to approval of shareholders in the annual general meeting.

Chief financial officer of Shaurya Limited has also presented the following information against corresponding relevant items in the balance sheet:

a) Property, Plant & Equipment consists a class of assets as office buildings whose carrying amount is ₹ 10,00,000. However, the fair value of said office building as on the date of transition is estimated to be ₹ 15,00,000. Company wants to follow revaluation model as its accounting policy in respect of its property, plant and equipment for the first annual Ind AS financial statements.

b) The fair value of Intangible assets as on the date of transition is estimated to be ₹ 2,50,000. However, the management is reluctant to incorporate the fair value changes in books of account.

c) Shaurya Ltd. had acquired 80% shares in a company, Excel private limited few years ago thereby acquiring the control upon it at that time. Shaurya Ltd. recognised goodwill as per erstwhile accounting standards by accounting the excess of consideration paid over the net assets acquired at the date of acquisition. Fair value exercise was not done at the time of acquisition.

d) Trade receivables include an amount of ₹ 20,000 as provision for doubtful debts measured in accordance with previous GAAP. Now as per latest estimates, the provision needs to be revised to ₹ 25,000.

e) Company had given a loan of ₹1,00,000 to an entity for the term of 10 years six years ago. Transaction costs were incurred separately for this loan. The loan carries an interest rate of 7%. The principal amount is to be repaid in equal installments over the period of ten years at the year end. Interest is also payable at each year end. The fair value of loan as on the date of transition is ₹ 50,000 as against the carrying amount of loan which at present amounts to ₹ 40,000. However, Ind AS 109 mandates to charge the interest expense as per effective interest method after the adjustment of transaction costs. Management says it is tedious task in the given case to apply the effective interest rate changes with retrospective effect and hence is reluctant to apply the same retrospectively in its first time adoption.

f) In the long term borrowings, ₹ 4,50,000 of component is due towards the State Government. Interest is payable on the government loan at 4%, however the prevailing rate in the market at present is 8%. The fair market value of loan stands at ₹ 4,20,000 as on the relevant date.

g) Under Previous GAAP, the mutual funds were measured at cost or market value, whichever is lower. Under Ind AS, the Company has designated these investments at fair value through profit or loss. The value of mutual funds as per previous GAAP is ₹ 2,00,000 as included in 'current investment'. However, the fair value of mutual funds as on the date of transition is ₹ 2,30,000.

h) Ignore separate calculation of deferred tax on above adjustments. Assume the net deferred tax income to be ₹ 50,000 on account of Ind AS transition adjustments.

Requirements:

- Prepare transition date balance sheet of Shaurya Limited as per Indian Accounting Standards
- Show necessary explanation for each of the items presented by chief financial officer in the form of notes, which may or may not require the adjustment as on the date of transition. **(20 Marks)**

5. (a) On 1 April 2019, entity A contracted for the construction of a building for ₹ 22,00,000. The land under the building is regarded as a separate asset and is not part of the qualifying asset. The building was completed at the end of March, 2020, and during the period the following payments were made to the contractor:

Payment date	**Amount (₹)**
1 April 2019	2,00,000
30 June 2019	6,00,000
31 December 2019	12,00,000
31 March 2020	2,00,000
Total	22,00,000

Entity A's borrowings at its year end of 31 March 2020 were as follows:

a. 10%, 4-year note with simple interest payable annually, which relates specifically to the project; debt outstanding on 31 March 2020 amounted to ₹ 7,00,000. Interest of ₹ 65,000 was incurred on these borrowings during the year, and interest income of ₹ 20,000 was earned on these funds while they were held in anticipation of payments.

b. 12.5% 10-year note with simple interest payable annually; debt outstanding at 1 April 2019 amounted to ₹ 10,00,000 and remained unchanged during the year; and

c. 10% 10-year note with simple interest payable annually; debt outstanding at 1 April 2019 amounted to ₹ 15,00,000 and remained unchanged during the year.

What amount of the borrowing costs can be capitalized at year end as per relevant Ind AS?

(6 Marks)

(b) Following are the Financial Statements of Abraham Ltd.:

Balance Sheet

Particulars	Note No.	As at 31 March, 2020 (₹ in lakh)
EQUITY AND LIABILITIES:		
Shareholders' funds		
Share capital (shares of ₹ 10 each)		1,000
Reserves and surplus	1	2,400
Non-current liabilities		
Long term borrowings	2	5,700
Deferred tax liabilities	3	400
Current liabilities		
Trade payables		300
Short-term provisions		300
Other current liabilities	4	200
Total		**10,300**
ASSETS		
Non-current assets		
Property, plant and equipment		5,000
Deferred tax assets	3	700
Current assets		
Inventories		1,500
Trade receivables	5	1,100
Cash and bank balances		2,000
Total		**10,300**

Statement of Profit & Loss

Particulars	Note No.	Year ended 31 March 2020 (₹ in lakh)
Revenue from operations		6,000
Expenses:		
Employee benefit expense		1,200
Operating costs		3,199
Depreciation		450
Total expenses		4,849
Profit before tax		1,151
Tax expense		201
Profit after tax		950

Notes to Accounts:

Note 1: Reserves and surplus **(₹ in lakh)**

Capital reserve		500
Surplus from P & L		
Opening balance	550	
Additions	950	1,500
Reserve for foreseeable loss		400
Total		2,400

Note 2: Long-term borrowings

Term loan from bank	5,700
Total	5,700

Note 3: Deferred tax

Deferred tax asset	700
Deferred tax liability	400
Total	300

Note 4: Other current liabilities

Unclaimed dividends	10
Billing in advance	150
Other current liabilities	40
Total	200

Note 5: Trade Receivables

Considered good (outstanding within 6 months)	1,065
Considered doubtful (due from past 1 year)	40
Provision for doubtful debts	(5)
Total	1,100

Additional information:

(i) Share capital comprises of 100 lakh shares of ₹ 10 each.

(ii) Term Loan from bank for ₹ 5,700 lakh also includes interest accrued and due of ₹ 700 lakh as on the reporting date.

(iii) Reserve for foreseeable loss is created against a service contract due within 6 months.

(iv) Inventory should be valued at cost ₹ 1,500 lakh, NRV as on date is ₹ 1,200 lakh.

(v) A dividend of 10% was declared by the Board of directors of the company.

(vi) Accrued Interest income of ₹ 300 lakh is not booked in the books of the company.

(vii) Deferred taxes related to taxes on income are levied by the same governing tax laws.

Identify and report the errors and misstatements in the above extracts and prepare corrected Balance Sheet and Statement of Profit & Loss and where required the relevant notes to the accounts with explanations thereof. **(14 Marks)**

6. (a) How will you recognize and present the grants received from the Government in the following cases as per Ind AS 20?

(i) A Ltd. received one acre of land to setup a plant in backward area (fair value of land

₹ 12 lakh and acquired value by Government is ₹ 8 lakhs).

(ii) B Ltd. received an amount of loan for setting up a plant at concessional rate of interest from the Government.

(iii) D Ltd. received an amount of ₹ 25 lakh for immediate start-up of a business without any condition.

(iv) S Ltd. received ₹ 10 lakh for purchase of machinery costing ₹ 80 lakh. Useful life of machinery is 10 years. Depreciation on this machinery is to be charged on straight line basis.

(v) Government gives a grant of ₹ 25 lakh to U Limited for research and development of medicine for breast cancer, even though similar medicines are available in the market but are expensive. The company is to ensure by developing a manufacturing process over a period of two years so that the cost comes down at least to 50%. **(5 Marks)**

(b) KK Ltd. runs a departmental store which awards 10 points for every purchase of ₹ 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 ₹ 0.50. During the accounting period 2019-2020, 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 ₹ 10,00,000 on a particular day?
(b)	How should the redemption transaction be recorded in the year 2019-2020? The Company has requested you to present the sale of goods and redemption as independent transaction. Total sales of the entity is₹ 5,000 lakhs.
(c)	How much of the deferred revenue should be recognized at the year-end (2019-2020) because of the estimation that only 80% of the outstanding points will be redeemed?
(d)	In the next year 2020-2021, 60% of the outstanding points were discounted. Balance 40% of the outstanding points of 2019-2020 still remained outstanding. How much of the deferred revenue should the merchant recognize in the year 2020-2021 and what will be the amount of balance deferred revenue?
(e)	How much revenue will the merchant recognized in the year 2021-2022, if 3,00,000 points are redeemed in the year 2021-2022?

(10 Marks)

(c) **EITHER**

An entity issues 2,000 convertible bonds at the beginning of Year 1. The bonds have a three-year term and are issued at par with a face value of ₹ 1,000 per bond, giving total proceeds of ₹ 20,00,000. Interest is payable annually in arrears at a nominal annual interest rate of 6%. Each bond is convertible at any time up to maturity into 250 ordinary shares. The entity has given an option to settle the principal amount of the convertible bonds in ordinary shares or in cash.

When the bonds are issued, the prevailing market interest rate for similar debt without a conversion option is 9%. At the issue date, the market price of one ordinary share is ₹ 3. Income tax is ignored.

Calculate basic and diluted EPS when

Profit attributable to ordinary equity holders of the parent entity Year 1	₹ 10,00,000
Ordinary shares outstanding	12,00,000
Convertible bonds outstanding	2,000

(5 Marks)

OR

ABC Ltd. is a long-standing customer of XYZ Ltd. Mrs. P whose husband is a director in XYZ Ltd. purchased a controlling interest in entity ABC Ltd. on 1 June 2019. Sales of products from XYZ Ltd. to ABC Ltd. in the two-month period from 1 April 2019 to 31 May 2019 totalled ₹ 8,00,000. Following the share purchase by Mrs. P, XYZ Ltd. began to supply the products at a discount of 20% to their normal selling price and allowed ABC Ltd. three months' credit (previously ABC Ltd. was only allowed one month's credit, XYZ Ltd.'s normal credit policy). Sales of products from XYZ Ltd. to ABC Ltd. in the ten-month period from 1 June 2019 to 31 March 2020 totalled ₹ 60,00,000. On 31 March 2020, the trade receivables of XYZ Ltd. included ₹ 18,00,000 in respect of amounts owing by ABC Ltd.

Analyse and show (where possible by quantifying amounts) how the above event would be reported in the financial statements of XYZ Ltd. for the year ended 31 March 2020 as per Ind AS. You are required to mention the disclosure requirements as well. **(5 Marks)**