Case study 1- Answers

I. Answers to Descriptive Questions

Answer 1

(a) In the present case, majority consent is required to conduct the relevant activities of C Ltd. A Ltd. has majority voting rights and decisions will be taken by the majority shareholders and A Ltd. also controls the relevant activities of C Ltd. by having control over costing, budgeting, pricing and marketing of the project. A Ltd. exercises control over this entity, it is exposed to variable returns from its involvement with C Ltd. and has the ability to affect those returns through its power over C Ltd. Therefore, considering the guidance under IFRS 10, A Ltd. might have to consolidate C Ltd. as its subsidiary.

(b) Since only three trustees out of ten, are closely related to A Ltd. who actively participate, and all trustees participate in their own capacity. Hence, A Ltd. doesn't have power over the trust. Further, donation given by A Ltd. to trust will never flow back to A Ltd. even in case of dissolution and discount allowed on tuition fee is also not material and not being borne by ABC Foundation. Hence, A Ltd. doesn't have any direct exposure, or rights, to variable returns of the trust. On analysis of the above facts and guidance available under IFRS 10, A Ltd. neither has power nor has exposure to variable returns. Thus, considering the requirement under IFRS 10, control could not be established. Thus, A Ltd. cannot consolidate ABC Foundation as its subsidiary under IFRS.

Answer 2

According to IFRS 9 criteria, A Ltd. and D Ltd. will classify the loan asset and liability, respectively, at amortised cost.

Scenario (a)

Since the loan is repayable on demand, it has fair value equal to cash consideration given. A Ltd. and D Ltd. should recognize financial asset and liability, respectively, at the amount of loan given. Upon, repayment, both the entities should reverse the entries that were made at the origination. It may be noted that this accounting outcome will not apply when there is evidence that the loan is repayable after a period of time, but is disguised as being repayable on demand. Consideration should be given to the substance of the arrangement.

Journal entries in the books of A Ltd.

At origination		
Loan to D Ltd. A/c	Dr.	INR 10,00,000
Bank A/c	Cr.	INR 10,00,000

On repayment		
Bank A/c	Dr.	INR 10,00,000
Loan to D Ltd. A/c	Cr.	INR 10,00,000

Journal entries in the books of D Ltd.

At origination		
Bank A/c	Dr.	INR 10,00,000
Loan from A Ltd. A/c	Cr.	INR 10,00,000

On repayment		
Loan from A Ltd. A/c	Dr.	INR 10,00,000
Bank A/c	Cr.	INR 10,00,000

Scenario (b)

Both A Ltd. and D Ltd. should recognise financial asset and liability, respectively, at fair value on initial recognition, i.e., the present value of INR 10,00,000 payable at the end of 3 years using discounting factor of 10%, i.e., INR 7,51,310. The difference between the loan amount and its fair value is treated as an equity contribution to the subsidiary. This represents a further investment by the parent in the subsidiary.

Journal entries in the books of A Ltd.

At origination		
Loan to D Ltd. A/c	Dr.	INR 7,51,315
Investment in A Ltd. A/c	Dr.	INR 2,48,685
Bank A/c	Cr.	INR 10,00,000

During periods to repayment- to recognise interest		
Year 1		
Loan to D Ltd. A/c	Dr.	INR 75,130
Interest income A/c	Cr.	INR 75,130
Year 2		
Loan to D Ltd. A/c	Dr.	INR 82,645
Interest income A/c	Cr.	INR 82,645
Year 3		
Loan to D Ltd. A/c	Dr.	INR 90,909
Interest income A/c	Cr.	INR 90,909
Note- Interest needs to be recognised in statement of profit and loss. The same cannot be adjusted against capital contribution recognised at origination.		

On repayment		
Bank A/c	Dr.	INR 10,00,000
Loan to D Ltd. A/c	Cr.	INR 10,00,000

Journal entries in the books of D Ltd.

At origination		
Bank A/c	Dr.	INR 10,00,000
Loan from A Ltd. A/c	Cr.	INR 7,51,130
Equity Contribution in A Ltd. A/c	Cr.	INR 2,48,690

During periods to repayment- to recognise interest		
Year 1		
Interest expense A/c	Dr.	INR 75,131
Loan from A Ltd. A/c	Cr.	INR 75,131
Year 2		
Interest expense A/c	Dr.	INR 82,645
Loan from A Ltd. A/c	Cr.	INR 82,645
Year 3		
Interest expense A/c	Dr.	INR 90,909
Loan from A Ltd. A/c	Cr.	INR 90,909

On repayment		
Loan from A Ltd. A/c	Dr.	INR 10,00,000
Bank A/c	Cr.	INR 10,00,000

Working Note:

Years	Amount outstanding (opening)	Interest	Amount outstanding (closing)
Beginning of year 1		-	INR 7,51,315
End of year 1	INR 7,51,315	INR 75,131	INR 8,26,446
End of year 2	INR 8,26,446	INR 82,645	INR 9,09,091
End of year 3	INR 9,09,091	INR 90,909	INR 10,00,000

Answer 3

(a) In present case, the said compressor's carrying amount will be recovered principally through sale and not through its continuing use. Further, the asset is retired from active use and it is kept idle, hence compressor is available for immediate sale in its present condition. Since the time, compressor was classified as 'assets held for disposal', A Ltd. was committed to sell the compressor and for such sale it invited global bids as well to fetch good price for such compressor. A Ltd. always had the intention of selling it immediately on receiving good price for the compressor. On receipt of bid from the buyer, U Ltd., A Ltd. initiated procedures to sell the compressor to him, but due to disagreement regarding currency of sales consideration at a later stage, a dispute arose between both the parties and the matter was taken to the Court, which later got transferred to the Arbitrator. Also a stay order has also been issued by the Court, restricting A Ltd. to sell the asset to any other party till the matter is resolved by the arbitrator, with whom case is currently pending. As a result, A Ltd. is not able to sell the compressor till the matter is resolved, pursuant to High Court's stay order. Till date, A Ltd. has complied with all the orders/ instructions received from the Court/ arbitrator and is awaiting arbitrator's verdict on this matter, which is expected to be July 2018. As on today, subject to the stay order, A Ltd. is still committed to sell the compressor. The compressor is currently not in use, but kept it idle, ready for sale. Hence, based on the facts of the case and considering the principles under IFRS 5, it can be said that A Ltd. is committed to sell the compressor but due to factors beyond the control of A Ltd., i.e., stay order from the Court, it is restricted from selling the compressor till the matter is resolved by the assigned arbitrator. Hence, till the matter is resolved, compressor should be classified as 'non-current assets held for sale'.

(b) As on 31 March 2015, in Indian GAAP audited financial statements of A Ltd., compressor is classified as 'assets held for disposal' and valued at lower of net book value (carrying amount) and net realisable value, i.e., INR 6,522,681 in the present case. As per the guidance under IFRS 5, non-current assets held for sale should be measured at lower of carrying amount and fair value *less* costs to sell. There is a difference between the term 'net realisable value' and 'fair value *less* costs to sell', i.e., net realisable value is an exit price for an asset, whereas fair value *less* costs to sell is an entry price, i.e., price to be paid for acquiring an asset. Considering the facts in the present case, one can infer that 'fair value *less* costs to sell' is greater than 'net realisable value'. Hence, in the opening IFRS balance sheet of A Ltd., compressor should be valued at carrying amount, since on 31 March 2015, carrying amount is less than net realisable value and net realisable value is less than fair value *less* costs to sell.

II. Answers to Objective Type Questions

1. Option (b) : INR 49,60,000

Value of 400 units of chemicals	400 x 10,000	INR 40,00,000
Value of 100 units of chemicals	100 x 9,600	INR 9,60,000
Value of stock on 31 March 2018		**INR 49,60,000**

Sale value on the reporting date is irrelevant as Net realisable value is the estimated selling price in the ordinary course of business less the estimated costs of completion and the estimated costs necessary to make the sale. NRV is not the selling price on the reporting date.

2. Option (d) : INR 27,00,000

Basic price (as per supplier's invoice plus taxes)	INR 20,00,000
Initial delivery and handling costs	INR 4,00,000
Cost of site preparation	INR 2,00,000

Interest charges paid to supplier of plant for deferred credit (since there is no qualifying asset)	-
Present value of estimated dismantling costs to be incurred after 10 years	INR 1,00,000
Operating losses before commercial production	-
Cost of machinery	**INR 27,00,000**

3. Option (a) : Deferred tax asset of INR 9,000

Particulars	**Carrying amount**	**Tax base**	**Temporary difference**
At acquisition	INR 1,50,000	INR 1,50,000	Nil
Accumulated depreciation	(INR 50,000)	(INR 50,000)	Nil
Impairment loss	(INR 30,000)	Nil	(INR 30,000)

Tax rate	30%
Deferred tax asset	INR 9,000

4. Option (d) : 20 months

Capitalisation under IAS 23 will commence from the date when the expenditure is incurred (1 May 2016) and must cease when the asset is ready for its intended use (28 February 2018); in this case a 22- month period. However, interest cannot be capitalised during a period where development activity is suspended ie for the period of two months from July, 2017 to August, 2017.

5. Option (c) : Impairment loss for the cash-generating unit of INR 1,00,000 should be first allocated to goodwill (i.e., INR 50,000) and balance impairment loss of INR 50,000 should be allocated on a pro-rata basis between the plant and machinery and technical know-how based on their carrying amounts, at INR 26,000 and INR 24,000, respectively.

6. Option (c) : Intangible asset of INR 2,00,000; expense of INR 8,00,000 (Refer para 65, 74 and 76 of IAS 38)

Research expenditure	Expense as incurred
Development expenditure	• Expense if the recognition criteria for intangible assets are not met • Capitalise once the recognition criteria are met • Past expense cannot be capitalised

7. Option (b) : Single Contract

8. Option (c) : A Ltd. should recognise an expense of INR 1,50,000 immediately and cannot reverse the expense recognised even if the director goes to work for a competitor and loses the share options.

The 'non-compete' clause is a non-vesting condition, because A Ltd. does not receive any services. On the grant date, A Ltd. should immediately recognise a cost of INR 1,50,000, as the director is not providing any future services. A Ltd. cannot reverse the expense recognised, even if the director goes to work for a competitor and loses the share options, because the condition is a non-vesting condition.

9. Option (c) : Current liability even if the lender agreed after reporting date and before authorisation of financial statements for issue, not to demand payment as a consequence.

If the entity has an unconditional right to defer the settlement of the liability for at least twelve months, the debt should be classified as non-current liability. In the given case, liability becomes payable on demand, therefore, it will be classified as current even if the lender agreed after reporting date and before authorisation of financials for issue, not to demand payment as a consequence.

10. Option (a) : INR 25 lacs

Particulars	**Amount**
Fair value of consideration	INR 60,00,000
Fair value of non-controlling interest	INR 45,00,000
	INR 1,05,00,000
Less: Fair value of net assets	(INR 80,00,000)
Goodwill	**INR 25,00,000**

Note:

Alternative answers may be possible for certain questions of the case study, depending upon the view taken.