MODEL TEST PAPER 5

FINAL COURSE: GROUP – I

PAPER – 1: FINANCIAL REPORTING

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

1. *The question paper comprises two parts, Part I and Part II.*
2. *Part I comprises Case Scenario based Multiple Choice Questions (MCQs)*
3. *Part II comprises questions which require descriptive type answers.*

PART I – Case Scenario based MCQs (30 Marks)

All MCQs are compulsory.

Case Scenario 1

ABC Ltd. maintains its accounts and prepares its annual financial statements in accordance with Indian Accounting Standards (Ind AS). It is a diversified global business group with operations spanning multiple sectors. The finance team while working on finalizing the books for the year ending 31st March, 20X3, encountered challenges with the following transactions:

(i) ABC Ltd. manufactures automobile parts. It has shown a net profit of ₹ 20,00,000 for the third quarter of 20X2-20X3.

Following adjustments are made while computing the net profit:

(1) Bad debts of ₹ 1,00,000 incurred during the quarter. 50% of the bad debts have been deferred to the next quarter.

(2) ₹ 5,00,000 expenditure on account of administrative expenses pertaining to the third quarter is deferred on the argument that the fourth quarter will have more sales; therefore, fourth quarter should be debited by higher expenditure. The expenditures are uniform throughout all quarters.

(ii) ABC Ltd. enters into a contract to build a power plant for a customer. The entity will be responsible for the overall management of the project including services to be provided like engineering, site clearance, foundation, procurement, construction of the structure, piping and wiring, installation of equipment and finishing.

(iii) In financial year 20X1-20X2, ABC Ltd. incurred the following expenditure in acquiring property consisting of 6 identical houses each with separate legal title including the land on which it is built.

The expenditure incurred on various dates is given below:

- On 1st April, 20X2 - Purchase cost of the property ₹ 1,80,00,000
- On 1st April, 20X2 – Non-refundable transfer taxes ₹ 20,00,000 (not included in the purchase cost)
- On 2nd April, 20X2- Legal cost related to property acquisition ₹ 5,00,000
- On 6th April, 20X2- Advertisement campaign to attract tenants ₹ 3,00,000
- On 8th April, 20X2- Opening ceremony function for starting business ₹ 1,50,000

Throughout 20X2-20X3, incurred ₹ 1,00,000 towards day-to-day repair maintenance and other administrative expenses.

ABC Ltd. uses one of the six houses for office and accommodation of its few staffs. The other five houses are rented to various independent third parties.

Analyze the transactions mentioned above and choose the most appropriate option in the below questions 1 to 6 in line with relevant Ind AS:

1. What will be the treatment of bad debts incurred during the third quarter?

   The treatment of bad debts is not correct as the expenses incurred during an interim reporting period should be recognised in the same period. Accordingly, ₹ 50,000 should be deducted from ₹ 20,00,000.

   (a) Bad debts expenses incurred during third quarter should be recognised in the same quarter. Accordingly, ₹ 50,000 should be deducted from ₹ 20,00,000.

   (b) Bad debts expenses incurred during third quarter should be recognised equally in the third and fourth quarter. Accordingly, the treatment done in the books is correct and no further adjustment in this regard is required.

(c) Bad debts expenses incurred during third quarter should be recognised at the end of the financial year in the last quarter. Accordingly, ₹ 50,000 already deducted should be added back from ₹ 20,00,000.

(d) No bad debt accounted in the interim financial statements in any of the quarter.

2. The correct net profits to be shown in Interim Financial Report of the third quarter shall be

(a) ₹ 15,00,000

(b) ₹ 20,00,000

(c) ₹ 19,50,000

(d) ₹ 14,50,000

3. How many performance obligations does the entity have?

(a) Three performance obligations

(b) Two performance obligations

(c) A single performance obligation

(d) More than three performance obligations

4. What is the cost of the entire property?

(a) ₹ 1,80,00,000

(b) ₹ 2,05,00,000

(c) ₹ 2,06,00,000

(d) ₹ 1,85,00,000

5. What is the cost of the investment property?

(a) ₹ 1,70,83,333

(b) ₹ 2,05,00,000

(c) ₹ 34,16,667

(d) ₹ 1,80,00,000

6. What is the cost of the owner-occupied property?

(a) ₹ 1,70,83,333

(b) ₹ 2,05,00,000

(c) ₹ 34,16,667

(d) ₹ 1,80,00,000 **(6 x 2 Marks = 12 Marks)**

Case Scenario 2

DEF Ltd. is a diversified business group operating in multiple business segments across different parts of the world with multiple subsidiaries. It maintains its books of accounts and publishes its annual financial statements under Indian Accounting Standards. The finance team has been working on closing the books of accounts and generating financial statements for the year ended 31st March 20X1 and are facing issues in the following transactions while finalization of financial statements:

(i)

Profit attributable to ordinary equity holders of the parent entity for year 20X1	₹ 1,200,000
Weighted average number of ordinary shares outstanding during year 20X1	500,000 shares
Average market price of one ordinary share during year 20X1	₹ 20.00
Weighted average number of shares under option during year 20X1	100,000 shares
Exercise price for shares under option during year 20X1	₹ 15.00

(ii) DEF Ltd. enters into a contract to buy 100 tonnes of cocoa beans at 1,000 per tonne for delivery in 12 months. On the settlement date, the market price for cocoa beans is 1,500 per tonne. The contract cannot be settled net in cash and is entered for delivery of cocoa beans in line with DEF Ltd.'s expected purchase/ usage requirements.

(iii) DEF Ltd. invests in compulsorily convertible preference shares (CCPS) issued by its subsidiary B Ltd. at ₹ 1,000 each (₹ 10 face value + ₹ 990 premium). Under the terms of the instrument, each CCPS is compulsorily convertible into one equity share of B Ltd at the end of 5 years. Such CCPS carry dividend @ 12% per annum, payable only when declared at the discretion of B Ltd.

Analyze the transactions mentioned above and choose the most appropriate option in the below questions 7 to 10 in line with relevant Ind AS:

7. Based on the facts given in scenario (i), what will be basic EPS of the entity?

   (a) 2.29

   (b) 2.40

   (c) 2.00

   (d) 1.77

8. Based on the facts given in scenario (i), what will be diluted EPS of the entity?

   (a) 2.29

   (b) 2.40

   (c) 2.00

   (d) 1.77

9. What is the nature of the contract entered into for cocoa beans?

   (a) Cash contract

   (b) Non-executory and derivative contract

   (c) Derivative contract

   (d) Executory and non-derivative contract

10. What is the nature of the financial instrument mentioned in point (iii)?

    (a) Financial Asset

    (b) Financial Liability

    (c) Equity

    (d) Not a financial instrument **(4 x 2 Marks = 8 Marks)**

Case Scenario 3

PQR Ltd. is required to adopt Ind AS from 1st April, 20X1, with comparatives for one year, i.e., for 20X0-20X1. On 1st April, 20X1, PQR Ltd. acquired 30% of the voting ordinary shares of XYZ Ltd. for ₹ 8,000 crore. PQR Ltd. accounts

its investment in XYZ Ltd. using equity method as prescribed under Ind AS 28. At 31st March, 20X2, PQR Ltd. recognised its share of the net asset changes of XYZ Ltd. using equity accounting as follows:

	(₹ in crore)
Share of profit or loss	700
Share of exchange difference in OCI	100
Share of revaluation reserve of PPE in OCI	50

The carrying amount of the investment in the associate on 31st March, 20X2 was therefore ₹ 8,850 crore (8,000 + 700 + 100 + 50).

On 1st April, 20X2, PQR Ltd. acquired the remaining 70% of XYZ Ltd. for cash ₹ 25,000 crore. The following additional information is relevant at that date:

	(₹ in crore)
Fair value of the 30% interest already owned	9,000
Fair value of XYZ's identifiable net assets	30,000

Analyze the transactions mentioned above and choose the most appropriate option in the below questions 11 to 15 in line with relevant Ind AS:

11. What is the fair value of the total consideration transferred by PQR Ltd. to XYZ Ltd.?

    (a) ₹ 34,000 crores

    (b) ₹ 33,850 crores

    (c) ₹ 33,000 crores

    (d) ₹ 25,000 crores

12. What is the amount of goodwill in the said business combination?

    (a) ₹ 3,000 crores

    (b) ₹ 4,000 crores

    (c) ₹ 2,150 crores

    (d) ₹ 3,850 crores

13. What is the gain on previously held interest in XYZ Ltd. recognised in profit or loss?

(a) ₹ 150 crores

(b) ₹ 100 crores

(c) ₹ 250 crores

(d) Nil

14. What is the transition date for PQR Ltd. for adopting Ind AS?

    (a) 1st April, 20X0

    (b) 1st April, 20X1

    (c) 1st April, 20X2

    (d) 1st April, 20X3

15. PQR Ltd. present its comparatives financial statements for the year-

    (a) 20X1-20X2

    (b) 20X2-20X3

    (c) 20X0-20X3

    (d) 20X0-20X1 **(5 x 2 Marks = 10 Marks)**

PART – II DESCRIPTIVE QUESTIONS

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.

Maximum Marks – 70 Marks

1. DEF Ltd. acquired 100% ordinary shares of ₹ 100 each of XYZ Ltd. on 1st October 20X1. On 31st March, 20X2 the summarised Balance Sheets of the two companies were as given below:

	DEF Ltd.	XYZ Ltd.
Assets		
Property Plant Equipment		
Land & Buildings	15,00,000	18,00,000
Plant & Machinery	24,00,000	13,50,000

Investment in XYZ Ltd.	34,00,000	-
Inventory	12,00,000	3,64,000
Financial Assets		
Trade Receivable	5,98,000	4,00,000
Cash	1,45,000	80,000
Total	**92,43,000**	**39,94,000**
Equity & Liabilities		
Equity Capital (Shares of ₹ 100 each fully paid)	50,00,000	20,00,000
Other Equity		
Other reserves	24,00,000	10,00,000
Retained Earnings	5,72,000	8,20,000
Financial Liabilities		
Bank Overdraft	8,00,000	-
Trade Payable	4,71,000	1,74,000
Total	**92,43,000**	**39,94,000**

The retained earnings of XYZ Ltd. showed a credit balance of ₹ 3,00,000 on 1st April 20X1 out of which a dividend of 10% was paid on 1st November; DEF Ltd. has recognised the dividend received to profit or loss account; Fair Value of P&M as on 1st October 20X1 was ₹ 20,00,000. The rate of depreciation on plant & machinery is 10%.

Following are the increases on comparison of fair value as per respective Ind AS with book value as on 1st October 20X1 which are to be considered while consolidating the Balance Sheets.

Liabilities	**Amount**	**Assets**	**Amount**
Trade Payables	1,00,000	Land & Buildings	10,00,000
		Inventories	1,50,000

Notes:

a) It may be assumed that the inventory is still unsold on balance sheet date and the Trade Payables are also not yet settled.

b) Also assume that the Other Reserves of both the companies as on 31st March 20X2 are the same as was on 1st April 20X1.

c) All fair value adjustments have not yet started impacting consolidated post-acquisition profits.

Prepare Consolidated Balance Sheet as at 31st March, 20X2.

(14 Marks)

2. (a) Wheel Co. Limited borrowed ₹ 500,000,000 from a bank on 1 January 20X1. The original terms of the loan were as follows:

- Interest rate: 11%
- Repayment of principal in 5 equal instalments
- Payment of interest annually on accrual basis
- Upfront processing fee: ₹ 5,870,096

Effective interest rate on loan: 11.50%

On 31 December 20X2, Wheel Co. Limited approached the bank citing liquidity issues in meeting the cash flows required for immediate instalments and re-negotiated the terms of the loan with banks as follows:

- Interest rate 15%
- Repayment of outstanding principal in 10 equal instalments starting 31 December 20X3
- Payment of interest on an annual basis

Record journal entries in the books of Wheel Co. Limited till 31 December 20X3, after giving effect of the changes in the terms of the loan on 31 December 20X2 **(10 Marks)**

(b) An entity manufactures passenger vehicles. The time between purchasing of underlying raw materials to manufacture the passenger vehicles and the date the entity completes the production and delivers to its customers is 11 months. Customers settle the dues after a period of 8 months from the date of sale.

(i) Will the inventory and the trade receivables be current in nature?

(ii) Assuming that the production time was say 15 months and the time lag between the date of sale and collection from customers is 13 months, will the answer be different?

(4 Marks)

3. (a) On 1st September, 20X1, entity X plans to sell a group of assets and liabilities, which is classified as a disposal group. On 31st October, 20X1, the Board of Directors approves and becomes committed to the plan to sell the manufacturing unit by entering into a firm purchase commitment with entity Y. 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 February, 20X2 and the sale is expected to be completed by 30th June, 20X2.

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

Particulars	**Carrying value as on 31st March, 20X1**	**Carrying value as on 31st October, 20X1**
Goodwill	500	500
Plant and Machinery	1,000	900
Building	2,000	1,850
Debtors	850	1,050
Inventory	700	400
Creditors	(300)	(250)
Loans	(2,000)	(1,850)
	2,750	2,600

The fair value of the manufacturing unit as on 31st March, 20X1 is ₹ 2,000 and as on 31st October, 20X1 is ₹ 1,850. The cost to sell is ₹ 100 on both these dates. The disposal group is not sold at the period end i.e., 31st March, 20X2. The fair value as on 31st March, 20X2 is lower than the carrying value of the disposal group as on that date.

1. Assess whether the manufacturing unit can be classified as held for sale and reasons there for. If yes, then at which date?

2. Measure the manufacturing unit on the date of classification as held for sale.

3. Measure the manufacturing unit at the end of the financial year. **(8 Marks)**

(b) On 30th January, 20X1, A Ltd. purchased a machinery for $ 5,000 from USA supplier on credit basis. A Ltd.'s functional currency is Rupees. The exchange rate on the date of transaction is 1 $ = ₹ 60. The fair value of the machinery determined on 31st March, 20X1 is $ 5,500. The exchange rate on 31st March, 20X1 is 1$ = ₹ 65. The payment to overseas supplier done on 31st March 20X2 and the exchange rate on 31st March 20X2 is 1$ = ₹ 67. The fair value of the machinery remains unchanged for the year ended on 31st March 20X2. Tax rate is 30%. A Ltd. follows revaluation method in respect of Plant & Machinery.

Pass the Journal entries for the year ended on 31st March 20X1 and year 20X2 according to Ind AS 21. **(6 Marks)**

4. (a) A Ltd. purchased some Property, Plant and Equipment on 1st April, 20X1, and estimated their useful lives for the purpose of financial statements prepared on the basis of Ind AS. Following were the original cost, and useful life of the various components of property, plant, and equipment assessed on 1st April, 20X1:

Property, Plant and Equipment	Original Cost	Estimated useful life
Buildings	₹ 15,000,000	15 years
Plant and machinery	₹ 10,000,000	10 years
Furniture and fixtures	₹ 3,500,000	7 years

A Ltd. uses the straight-line method of depreciation. On 1st April, 20X4, the entity reviewed the following useful lives of the property, plant, and equipment through an external valuation expert:

Buildings	10 years
Plant and machinery	7 years
Furniture and fixtures	5 years

There were no salvage values for the three components of the property, plant, and equipment either initially or at the time the useful lives were revised.

Examine the impact of revaluation of useful life on the Statement of Profit and Loss for the year ending 31st March, 20X5. **(6 Marks)**

(b) P Ltd. granted 400 stock appreciation rights (SAR) each to 75 employees on 1st April 20X1 with a fair value ₹ 200. The terms of the award require the employee to provide service for four years in order to earn the award. The fair value of each SAR at each reporting date is as follows:

31st March 20X2	₹ 210
31st March 20X3	₹ 220
31st March 20X4	₹ 215
31st March 20X5	₹ 218

What would be the difference if at the end of the second year of service (i.e. at 31st March 20X3), P Ltd. modifies the terms of the award to require only three years of service? **(8 Marks)**

5. (a) AST Limited enters into a contract with a customer to build a manufacturing facility. The entity determines that the contract contains one performance obligation satisfied over time.

Construction is scheduled to be completed by the end of the 36th month for an agreed-upon price of ₹ 25 crore.

The entity has the opportunity to earn a performance bonus for early completion as follows:

- 15 percent bonus of the contract price if completed by the 30th month (25% likelihood)
- 10 percent bonus if completed by the 32nd month (40% likelihood)
- 5 percent bonus if completed by the 34th month (15% likelihood)

In addition to the potential performance bonus for early completion, AST Limited is entitled to a quality bonus of ₹ 2 crore if a health and safety inspector assigns the facility a gold star rating

as defined by the agency in the terms of the contract. AST Limited concludes that it is 60% likely that it will receive the quality bonus.

Determine the transaction price. **(6 Marks)**

(b) Mumbai Challengers Ltd., a listed entity, is a sports organization owning several cricket and hockey teams. The issues below pertain to the reporting period ending 31 March 20X2.

Mumbai Challengers Ltd. acquires and sells players' registrations on a regular basis. For a player to play for its team, Mumbai Challengers Ltd. must purchase registrations for that player. These player registrations are contractual obligations between the player and the company. The costs of acquiring player registrations include transfer fees, league levy fees, and player agents' fees incurred by the club.

At the end of each season, which happens to also be the reporting period end for Mumbai Challengers Ltd., the club reviews its contracts with the players and makes decisions as to whether they wish to sell/transfer any players' registrations. The company actively markets these registrations by circulating with other clubs a list of players' registrations and their estimated selling price. Players' registrations are also sold during the season, often with performance conditions attached. In some cases, it becomes clear that a player will not play for the club again because of, for example, a player sustaining a career threatening injury or being permanently removed from the playing squad for any other reason. The playing registrations of certain players were sold after the year end, for total proceeds, net of associated costs, of ₹ 175 crores. These registrations had a net book value of ₹ 49 crores.

Mumbai Challengers Ltd. seeks your advice on the treatment of the acquisition, extension, review and sale of players' registrations in the circumstances outlined above. **(4 Marks)**

(c) Explain the five fundamental principles of ethics for Chartered Accountants. **(4 Marks)**

6\. (a) (i) Entity A owns 250 ordinary shares in company XYZ, an unquoted company. Company XYZ has a total share capital of 5,000 shares with nominal value of ₹ 10. Entity XYZ's after-tax maintainable profits are estimated at ₹ 70,000 per

year. An appropriate price/earnings ratio determined from published industry data is 15 (before lack of marketability adjustment). Entity A's management estimates that the discount for the lack of marketability of company XYZ's shares and restrictions on their transfer is 20%. Entity A values its holding in company XYZ's shares based on earnings. Determine the fair value of Entity A's investment in XYZ's shares.

(ii) Based on the facts given in the aforementioned part (i), assume that, Entity A estimates the fair value of the shares it owns in company XYZ using a net asset valuation technique. The fair value of company XYZ's net assets including those recognised in its balance sheet and those that are not recognised is ₹ 8,50,000. Determine the fair value of Entity A's investment in XYZ's shares.

(5 Marks)

(b) **Either**

Following is a snapshot of audited balance sheet of company A as on 31st March 2014. Company A's equity shares are listed on Bombay Stock Exchange since 2010.

Liabilities	**₹ in crores**	**Assets**	**₹ in crores**
Equity Share Capital	160	Fixed Assets	455
Securities Premium	200	Investments	200
General Reserve	150	Current Assets	50
Revaluation Reserve	40	Miscellaneous Expenditure not written off	80
Profit and Loss A/c	75		
Liabilities	160		
Total	**785**	**Total**	**785**

As per roadmap, which Phase company A fall into? Will your answer change if Company A is an unlisted company? **(5 Marks)**

Or

As at 31st March 20X2, Natasha Ltd. carried trade receivables of ₹ 280 crores in its balance sheet. At that date, Natasha Ltd. entered into a factoring agreement with Samantha Ltd., a financial institution, according to which it transferred the trade receivables in exchange for an immediate cash payment of ₹ 250 crores. As per the factoring agreement, any shortfall between the amount collected and ₹ 250 crores will be reimbursed by Natasha Ltd. to Samantha Ltd. Once the trade receivables have been collected, any amounts above ₹ 250 crores, less interest on this amount, will be repaid to Natasha Ltd. The directors of Natasha Ltd. are of the opinion that the trade receivables should be derecognized.

You are required to explain the appropriate accounting treatment of this transaction in the financial statements for the year ending 31st March 20X2, and also evaluate this transaction in the context of the Conceptual Framework. **(5 Marks)**

(c) Under new legislation, an entity is required to fit smoke filters to its factories by 30th September, 20X1. The entity has not fitted the smoke filters. It is assumed that a reliable estimate can be made of any outflows expected.

Determine whether any provision is required to be made by the entity on

(a) At 31st March, 20X1, the end of the reporting period

(b) At 31st March, 20X2, the end of the reporting period

(4 Marks)