IND AS - 36

1.

Good Drugs and Pharmaceuticals Ltd. acquired a sachet filling machine on 1st April, 2016 for ₹ 60 lakhs. The machine was expected to have a productive life of 6 years. At the end of financial year 2016-2017 the carrying amount was ₹ 41 lakhs. A short circuit occurred in this financial year but luckily the machine did not get badly damaged and was still in working order at the close of the financial year. The machine was expected to fetch ₹ 36 lakhs, if sold in the market. The machine by itself is not capable of generating cash flows. However, the smallest group of assets comprising of this machine also, is capable of generating cash flows of ₹ 54 crore per annum and has a carrying amount of ₹ 3.46 crore. All such machines put together could fetch a sum of ₹ 4.44 crore if disposed. Discuss the applicability of Impairment loss.

Answer

As per provisions of Para 91(b) of AS 28 "Impairment of Assets", impairment loss is not to be recognized for a given asset if its cash generating unit (CGU) is not impaired. In the given question, the related cash generating unit which is group of asset to which the damaged machine belongs is not impaired; and the recoverable amount is more than the carrying amount of group of assets. Hence there is no need to provide for impairment loss on the damaged sachet filling machine.

2.

G Ltd., acquired a machine on 1st April, 2010 for ₹ 7 crore that had an estimated useful life of 7 years. The machine is depreciated on straight line basis and does not carry any residual value. On 1st April, 2014, the carrying value of the machine was reassessed at ₹ 5.10 crore and the surplus arising out of the revaluation being credited to revaluation reserve. For the year ended March 2016, conditions indicating an impairment of the machine existed and the amount recoverable ascertained to be only ₹ 79 lakhs. You are required to calculate the loss on impairment of the machine and show how this loss is to be treated in the books of G Ltd. G Ltd., had followed the policy of writing down the revaluation surplus by the increased charge of depreciation resulting from the revaluation.

Answer

Statement Showing Impairment Loss

	(₹ in crores)
Carrying amount of the machine as on 1st April 2010	7.00
Depreciation for 4 years i.e. 2010-2011 to 2013-2014 $\left[\frac{7\text{crores}}{7\text{years}} \times 4\text{years}\right]$	(4.00)
Carrying amount as on 31.03.2014	3.00
Add: Upward Revaluation (credited to Revaluation Reserve account)	2.10
Carrying amount of the machine as on 1st April 2014 (revalued)	5.10
Less: Depreciation for 2 years i.e. 2014-2015 & 2015-2016 $\left[\frac{5.10\text{ crores}}{3\text{ years}} \times 2\text{ years}\right]$	(3.40)
Carrying amount as on 31.03.2016	1.70
Less: Recoverable amount	(0.79)

Impairment loss		0.91
Less: Balance in revaluation reserve as on 31.03.2016:		
Balance in revaluation reserve as on 31.03.2014	2.10	
Less: Enhanced depreciation met from revaluation reserve 2014-2015 & 2015-2016 =[(1.70 – 1.00) x 2 years]	(1.40)	
Impairment loss set off against revaluation reserve balance as per para 58 of AS 28 "Impairment of Assets"		(0.70)
Impairment Loss to be debited to profit and loss account		0.21

IND AS 38

3.

U.K. International Ltd. is developing a new production process. During the financial year ending 31st March, 2016, the total expenditure incurred was ₹ 50 lakhs. This process met the criteria for recognition as an intangible asset on 1st December, 2015. Expenditure incurred till this date was ₹ 22 lakhs. Further expenditure incurred on the process for the financial year ending 31st March, 2017 was ₹ 80 lakhs. As at 31st March, 2017, the recoverable amount of know-how embodied in the process is estimated to be ₹ 72 lakhs. This includes estimates of future cash outflows as well as inflows.

You are required to calculate:

(i) Amount to be charged to Profit and Loss A/c for the year ending 31st March, 2016 and carrying value of intangible as on that date.

(ii) Amount to be charged to Profit and Loss A/c and carrying value of intangible as on 31st March, 2017.

Ignore depreciation.

Answer

As per AS 26 'Intangible Assets'

(i) For the year ending 31.03.2016

(1) Carrying value of intangible as on 31.03.2016:

At the end of financial year 31st March 2016, the production process will be recognized (i.e. carrying amount) as an intangible asset at a cost of ₹ 28 lakhs (expenditure incurred since the date the recognition criteria were met, i.e., from 1st December 2015).

(2) Expenditure to be charged to Profit and Loss account:

The ₹ 22 lakhs is recognized as an expense because the recognition criteria were not met until 1st December 2016. This expenditure will not form part of the cost of the production process recognized in the balance sheet.

(ii) For the year ending 31.03.2017

(1) Expenditure to be charged to Profit and Loss account:

	(₹ in lakhs)
Carrying Amount as on 31.03.2016	28
Expenditure during 2016 – 2017	80
Total book cost	108
Recoverable Amount	(72)
Impairment loss	36

₹ 36 lakhs to be charged to Profit and loss account for the year ending 31.03.2017.

(2) Carrying value of intangible as on 31.03.2017:

	(₹ in lakhs)
Total Book Cost	108
Less: Impairment loss	(36)
Carrying amount as on 31.03.2017	72

IND AS 19

4.

An employee, Darshan, has joined a company PQR Ltd. in the year 2014. The annual emoluments of Darshan as decided is ₹ 15,52,303.

The company also has a policy of giving a lump sum payment of 25% of the last drawn salary of the employee for each completed year of service, if the employee retires after completing minimum 5 years of service. The salary of the Darshan is expected to grow @ 10% per annum.

The company has inducted Darshan in the beginning of the year and it is expected that he will complete the minimum five-year term before retiring.

What is the amount the company should charge in its Profit and Loss account every year as cost for the Defined-Benefit Obligation? Also calculate service cost and the interest cost to be charged per year assuming a discount rate of 8%.

(P.V factor for 8% - 0.735, 0.794, 0.857, 0.926, 1)

Answer

(a) Calculation of Defined Benefit Obligation

If Darshan will complete minimum 5 year term, then it is assumed that he will retire in the 6th year.

Accordingly, Expected last drawn salary in the 6th year

= ₹ 15,52,303 x 110% x 110% x 110% x 110% x 110% = ₹ 25,00,000

Defined Benefit Obligation (DBO) = ₹ 25,00,000 x 25% x 5 = ₹ 31,25,000

Amount of ₹ 6,25,000 will be charged to Profit and Loss Account of the company every year as cost for Defined Benefit Obligation.

Calculation of Current Service Cost to be charged per year

Year	Equal apportioned amount of DBO [i.e. ₹ 31,25,000/5 years]	PV factor Discounting @ 8%	Current service cost (Present Value)
a	b	c	d = b x c
1	6,25,000	0.735 (4 Years)	4,59,375
2	6,25,000	0.794 (3 Years)	4,96,250
3	6,25,000	0.857 (2 Years)	5,35,625
4	6,25,000	0.926 (1 Year)	5,78,750
5	6,25,000	1 (0 Year)	6,25,000

Calculation of Interest Cost to be charged per year

Year	Opening balance	Interest cost	Current service cost	Closing balance
a	B	c = b x 8%	d	e = b + c + d
1	0	0	4,59,375	4,59,375
2	4,59,375	36,750	4,96,250	9,92,375
3	9,92,375	79,390	5,35,625	16,07,390
4	16,07,390	1,28,591	5,78,750	23,14,731
5	23,14,731	1,85,269*	6,25,000	31,25,000

*Due to approximations used in calculation, this figure is adjusted accordingly.

Note:

1. The question states that Darshan will complete minimum 5 year term. Accordingly, in the above solution, it is assumed that his retirement from service will be in the 6th year.
2. The above solution has been given assuming that the last drawn salary implies in the question is the annual emolument. However, alternatively one may assume last drawn salary as monthly salary. In such a situation the answer will be as follows:

Calculation of Defined Benefit Obligation

If Darshan will complete minimum 5 year term, then it is assumed that he will retire in the 6th year.

Accordingly, Expected last drawn salary in the 6th year

= ₹ 15,52,303 x 110% x 110% x 110% x 110% x 110% = ₹ 25,00,000

Defined Benefit Obligation (DBO) = (₹ 25,00,000/12) x 25% x 5 = ₹ 2,60,417

Amount of ₹ 52,083 (2,60,417 / 5) will be charged to Profit and Loss Account of the company every year as cost for Defined Benefit Obligation.

Calculation of Current Service Cost to be charged per year

Year	*Equal apportioned amount of DBO [i.e. ₹ 2,60,417 / 5 years]*	*Discounting @ 8% PV factor*	*Current service cost (Present Value)*
a	*b*	*c*	*d = b x c*
1	52,083	0.735 (4 Years)	38,281
2	52,083	0.794 (3 Years)	41,354
3	52,083	0.857 (2 Years)	44,635
4	52,083	0.926 (1 Year)	48,229
5	52,083	1 (0 Year)	52,083

Year	*Opening balance*	*Interest cost*	*Current service cost*	*Closing balance*
a	*b*	*c = b x 8%*	*d*	*e = b + c + d*
1	0	0	38,281	38,281
2	38,281	3,063	41,354	82,698
3	82,698	6,616	44,635	1,33,949
4	1,33,949	10,716	48,229	1,92,894
5	1,92,894	15,440*	52,083	2,60,417

*Due to approximations used in calculation, this figure is adjusted accordingly.

IND AS 108 5.

Test your understanding 2 – Identifying reportable segments

The 10% tests

Segment	10% total revenue (W1)	10% results test (W2)	10% assets (W3)	Report?
Europe	Y	Y	Y	Y
Middle East	N	N	N	N
Asia	Y	Y	N	Y
North America	Y	Y	Y	Y
Central America	N	N	N	N
South America	N	N	N	N

Based on the 10% tests, Europe, Asia and North America are reportable. However, we must check whether they comprise at least 75% of the company's external revenue.

The 75% test

	External revenue $000
Europe	140
Asia	150
North America	195
Total	485

The external revenue of reportable segments is 79% ($485,000/ $612,000) of total external revenue. The 75% test is met and no other segments need to be reported.

Conclusion

The reportable segments are Europe, Asia and North America.

(W1) **10% of total sales**

10% × $1m = $100,000.

All segments whose total sales exceed $100,000 are reportable.

(W2) 10% of results

10% of profit making segments:

10% × ($98,000 + $47,000 + $121,000 + $12,000) = $27,800

10% of loss making segments:

10% × ($26,000 + $15,000) = $4,100

Therefore, all segments which make a profit or a loss of greater than $27,800 are reportable.

(W3) 10% of total assets

10% × $10m = $1m.

All segments whose assets exceed $1m are reportable.

IND AS 115

6.

Example 11

Retailer has a customer loyalty programme. A customer is rewarded with ten loyalty point for every Rs 100 of purchases. Each point is redeemable at Re 1 on any future purchases of the Retailer's products within 3 years. During a reporting period, customers purchase products for Rs 200,000 and earn 20,000 points. The stand-alone selling price of the purchased products is Rs 200,000. Retailer expects 19,000 points to be redeemed. Retailer estimates a stand-alone selling price of Rs 0.95 per point (totalling Rs 19,000) on the basis of an estimate of the redemption. Thus the loyalty points are valued to reflect the discount the customer would obtain in the future and the likelihood of breakage in the loyalty points.

The points provide a material right to customers only on entering into a contract. Consequently, the points are a separate performance obligation. Retailer allocates the transaction price (Rs 200,000) to the product and the points on a relative stand-alone selling price basis as follows:

Product	182,648 [Rs 200,000 × (Rs 200,000 ÷ Rs 219,000)]
Points	17,352 [Rs 200,000 × (Rs 19,000 ÷ Rs 219,000)]

At the end of the first reporting period, 9000 points have been redeemed. Retailer continues to expect 19,000 points to be redeemed in total. Retailer recognises revenue for the loyalty points of Rs 8,220 [(9,000 points ÷ 19,000 points) × Rs 17,352]. Retailer recognizes total revenue of Rs 190868. However it has received consideration of Rs 200,000, it therefore recognizes a contract liability of Rs 9132 (200,000-190868) or (17352-8220) for the unredeemed points at the end of the first reporting period.

At the end of the second reporting period, 17,000 points have been redeemed cumulatively. Retailer updates its estimate of the points that will be redeemed. It now expects that 19,400 points will be redeemed. Retailer recognises revenue for the loyalty points of Rs 6,986 {[(17,000 total points redeemed ÷ 19,400 total points expected to be redeemed) × Rs 17,352 initial allocation] – Rs 8,220 recognised in the first reporting period}. The contract liability balance is Rs 2,146 (Rs 17,352 initial allocation – Rs 15,206 of cumulative revenue recognised).

At the end of the third reporting period, only 1000 points are redeemed, and the remaining 1400 points expire. Retailer will recognize the balance revenue of Rs 2,146 by releasing the entire contract liability.

7.

Test your understanding 2 – Shred Co

Shred Co sells a machine and one year's free technical support for $100,000. It usually sells the machine for $95,000 but does not sell technical support for this machine as a stand-alone product. Other support services offered by Shred Co attract a mark-up of 50%. It is expected that the technical support will cost Shred Co $20,000.

Required:

How should the transaction price be allocated between the machine and the technical support?

Test your understanding 2 – Shred Co

The selling price of the machine is $95,000 based on observable evidence.

There is no observable selling price for the technical support. Therefore, the stand-alone selling price needs to be estimated. One approach for this is to use the expected costs plus a margin. Based on this, the selling price of the service would be $30,000 ($20,000 × 150%).

The total standalone selling prices of the machine and support are $125,000 ($95,000 + $30,000). However, total consideration receivable is only $100,000. This means that the customer is receiving a discount for purchasing a bundle of goods and services of 20% ($25,000/$125,000).

IND AS 115 says that an entity must consider whether the discount relates to the whole bundle or to a particular performance obligation. In the absence of additional information, it is assumed here that it relates to the whole bundle.

The transaction price allocated to the machine is $76,000 ($95,000 × 80%).

The transaction price allocated to the technical support is $24,000 ($30,000 × 80%).

The revenue will be recognised as and when the performance obligations are satisfied.

8.

Test your understanding 3 – Clarence

Clarence entered into the following sale transactions during the year:

(a) On 1 January 20X1, Clarence sold its head office to Seedorf, a finance company, for $5 million. Clarence continued to use the asset and was responsible for the insurance and maintenance of the building. Clarence has the right to repurchase it for $6.05 million on 1 January 20X3, representing a 10% growth in value each year. At 1 January 20X1 the head office was valued at $11 million, with the carrying amount shown at $4 million. This value is expected to increase by January 20X3.

(b) On 31 December 20X1, Clarence sells a machine plus spare parts to Edgar for $500,000. The value of the machine was $480,000, with the value of the spare parts being $20,000. Clarence delivered the machine on 31 December, but was asked to hold the spare parts by Edgar, due to Clarence's warehouse being in close proximity to Edgar's factory. Clarence expects to hold the spare parts for 2-4 years.

The parts are kept separately in the warehouse, cannot be used or sold by Clarence, and are ready for immediate shipment at Edgar's request. Clarence agreed to the transaction as it decided that holding costs would be insignificant.

Required:

Explain the financial reporting treatment for the issues for the year ended 31 December 20X1.

Test your understanding 3 – Clarence

(a) The scenario indicates that control of the head office has not passed to Seedorf. Clarence has retained use of the office, as well as responsibility for maintaining and insuring it.

In addition to this, the sale has been made at a value significantly lower than the market value. The option to repurchase is also significantly below the market value. Therefore this should not be treated as a sale.

The head office should not be removed from the financial statements of Clarence. The $5 million should be treated as a loan, with 10% interest recorded on it each year. Therefore for the year ended 31 December 20X1 $500,000 ($5m × 10%) should be recorded in finance costs.

(b) This is a bill-and-hold arrangement. Even though Clarence retains physical possession of the goods, Edgar retains control. This can be seen in the fact that Clarence cannot use or sell the goods, and must ship them immediately upon Edgar's request.

In this arrangement there are potentially three performance obligations. These will be the provision of the machine and the spare parts, and the storage of the spare parts.

The performance obligations to provide the machine and the spare parts appear to be met on 31 December 20X1, so the full $500,000 revenue can be recognised.

If the storage of the parts had been deemed to be significant, and therefore part of the transaction price, the price related to this performance obligation would be separately recognised over the expected period of holding the parts.

Ind AS – 7

1.

Extracts from the consolidated financial statements of the AH Group for the year ended 30 June 20X5 are given below:

Consolidated statement of profit or loss for the year ended 30 June 20X5

	$000
Revenue	85,000
Cost of sales	(60,750)
Gross profit	24,250
Operating expenses	(5,650)
Profit from operations	18,600
Finance cost	(1,400)
Profit before disposal of property	17,200
Disposal of property (note 2)	1,250
Profit before tax	18,450
Tax	(6,250)
Profit for the period	12,200
Attributable to:	
Non-controlling interest	405
Owners of the parent	11,795
	12,200

Note: There were no items of other comprehensive income

Statement of financial position, with comparatives, at 30 June 20X5

		20X5		20X4
	$000	$000	$000	$000
Non-current assets				
Property, plant and equipment	50,600		44,050	
Goodwill (note 3)	5,910		4,160	
		56,510		48,210
Current assets				
Inventories	33,500		28,750	
Trade receivables	27,130		26,300	
Cash and cash equivalents	1,870		3,900	
		62,500		58,950
		119,010		107,160
Equity and liabilities	$000	$000	$000	$000
Equity shares	20,000		18,000	
Share premium	12,000		10,000	
Retained earnings	24,135		18,340	
		56,135		46,340
Non-controlling interest		3,875		1,920
Total equity		60,010		48,260
Non-current liabilities				
Interest-bearing borrowings		18,200		19,200
Current liabilities				
Trade payables	33,340		32,810	
Interest payables	1,360		1,440	
Tax	6,100		5,450	
		40,800		39,700
		119,010		107,160

Notes:

(1) Several years ago, AH acquired 80% of the issued equity shares of its subsidiary, BI. On 1 January 20X5, AH acquired 75% of the issued equity shares of CJ in exchange for a fresh issue of 2 million of its own $1 equity shares (issued at a premium of $1 each) and $2 million in cash. The net assets of CJ at the date of acquisition were assessed as having the following fair values:

	$000
Property, plant and equipment	4,200
Inventories	1,650
Trade receivables	1,300
Cash and cash equivalents	50
Trade payables	(1,950)
Tax	(250)
	5,000

(2) During the year, AH disposed of property, plant and equipment for proceeds of $2,250,000. The carrying value of the asset at the date of disposal was $1,000,000. There were no other disposals of property, plant and equipment. Depreciation of $7,950,000 was charged to the consolidated statement of profit or loss in the year.

(3) Goodwill on acquisition relates to the acquisition of two subsidiaries. Entity BI was acquired many years ago, and goodwill relating to this acquisition was calculated on a proportion of net assets basis. Goodwill relating to the acquisition of entity CJ during the year was calculated on the full goodwill basis. On 1 January 20X5 when CJ was acquired, the fair value of the non-controlling interest was $1,750,000. Any impairment of goodwill during the year was accounted for within operating expenses.

Required:

Prepare the consolidated statement of cash flows of the AH Group for the year ended 30 June 20X5 using the indirect method.

Solution:

Consolidated statement of cash flows for the year ended 30 June 20X5

	$000	$000
Cash flows from operating activities		
Profit before tax	18,450	
Less: profit on disposal of property (2,250 – 1,000)	(1,250)	
Add: finance cost	1,400	
Adjustment for non-cash items dealt with in arriving at operating profit:		
Depreciation	7,950	
Decrease in trade receivables (27,130 – 26,300 – 1,300)	470	
Increase in inventories (33,500 – 28,750 – 1,650)	(3,100)	
Decrease in trade payables (33,340 – 32,810 – 1,950)	(1,420)	
Goodwill impaired (W5)	1,000	
Cash generated from operations	23,500	
Income taxes paid (W2)	(5,850)	
Net cash from operating activities		**17.650**
Cash flows from investing activities		
Acquisition of subsidiary net of cash acquired (2,000 – 50)	(1,950)	
Purchase of property, plant, and equipment (W3)	(11,300)	
Proceeds from sale of property	2,250	
Net cash used in investing activities		(11,000)

Cash flows from financing activities		
Repayment of long-term borrowings (18,200 – 19,200)	(1,000)	
Dividend paid by parent (W7)	(6,000)	
Dividends paid to NCI (W6)	(200)	
Interest Paid (W1)	**(1,480)**	
Net cash used in financing activities		**(8,680)**
Net decrease in cash and cash equivalents		(2,030)
Cash and cash equivalents at 1 July 20X4		3,900
Cash and cash equivalents at 30 June 20X5		1,870

(W1) **Interest paid**

	$000
Bal b/fwd	1,440
Profit or loss	1,400
Interest paid (bal. fig.)	(1,480)
Bal c/fwd	1,360

(W2) **Income taxes paid**

	$000
Bal b/fwd	5,450
Profit or loss	6,250
New subsidiary	250
Tax paid (bal. fig.)	(5,850)
Bal c/fwd	6,100

(W3) **Property, plant and equipment**

	$000
Bal b/fwd	44,050
New subsidiary	4,200
Depreciation	(7,950)
Disposals	(1,000)
Additions (bal. fig.)	11,300
Bal c/fwd	50,600

(W4) **Goodwill arising on acquisition of subsidiary**

	$000
Fair value of shares issued (2m × $2)	4,000
Cash consideration	2,000
	6,000
Fair value of NCI at acquisition	1,750
	7,750
Fair value of net assets at acquisition	(5,000)
Goodwill at acquisition	2,750

(W5) **Goodwill**

	$000
Bal b/fwd	4,160
Goodwill on sub acquired (W4)	2,750
Impairment in year (bal. fig.)	(1,000)
Bal c/fwd	5,910

(W6) **Non-controlling interest**

	$000
Bal b/fwd	1,920
NCI arising on subsidiary acquired	1,750
Profit or loss	405
Dividend paid (bal. fig.)	(200)
Bal c/fwd	3,875

(W7) **Retained earnings**

	$000
Bal b/fwd	18,340
Profit or loss	11,795
Dividend paid (bal. fig.)	(6,000)
Bal c/fwd	24,135

IND AS 102

1.

Use Employee Benefit expense a/c in the place of Employee compensation exp

Use share based payment reserve a/c in the place of employee stock option outstanding a/c

The following particulars in respect of stock options granted by a company are available:

Number of shares	*4,00,000*
Grant date	*April 1, 2010*
Number of employees covered	*600*
Number of options granted per employee	*100*
Vesting condition: Continuous employment for 3 years	
Nominal value per share (₹)	*10*
Exercise price per share (₹)	*45*
Vesting date	*March 31, 2013*
Exercise Date	*May 31, 2014*
Fair value of option per share on grant date (₹)	*15*

Position on 31/03/11

(a) Number of employees expected to satisfy service condition = 540

(b) Number of employees left = 15

(c) Profit before amortisation of ESOP cost = ₹ 11.90 lakh

(d) Fair value per share = ₹ 60

Position on 31/03/12

(a) Number of employees expected to satisfy service condition = 552

(b) Number of employees left = 20

(c) Profit before amortisation of ESOP cost = ₹ 12.62 lakh

(d) Fair value per share = ₹ 66

Position on 31/03/13

(a) Number of employees left = 11

(b) Number of employees entitled to exercise option = 554

(c) Profit before amortisation of ESOP cost = ₹ 13.79 lakh

(d) Fair value per share = ₹ 72

Position on 31/05/14

(a) Number of employees exercising the option = 550

(b) Number of employees not exercising the option = 4

Show Employees Compensation A/c, ESOP Outstanding A/c from 2010-11 to 2013-14.

Compute basic and diluted EPS for the years 2010-11 to 2012-13.

Solution

Year 2010-11

Fair value of option per share = ₹ 15

Number of options expected to vest under the scheme = 540 × 100 = 54,000

Fair value = 54,000 × ₹ 15 = ₹ 8,10,000

Vesting period = 3 years

Value of option recognised as expense in 2010-11 = ₹ 8,10,000 / 3 = ₹ 2,70,000

Year 2011-12

Fair value of option per share = ₹ 15

Number of options expected to vest under the scheme = 552 × 100 = 55,200

Fair value = 55,200 × ₹ 15 = ₹ 8,28,000

Vesting period = 3 years

Number of years expired = 2 years

Cumulative value of option to recognise as expense in 2010-11 and 2011-12

= (₹ 8,28,000/ 3) × 2 = ₹ 5,52,000

Value of option recognised as expense in 2011-12

= ₹ 5,52,000 – ₹ 2,70,000 = ₹ 2,82,000

Year 2012-13

Fair value of option per share = ₹ 15

Number of options actually vested under the scheme = 554 × 100 = 55,400

Fair value = 55,400 × ₹ 15 = ₹ 8,31,000

Cumulative value of option to recognise as expense in 3 years = ₹ 8,31,000

Value of option recognised as expense in 2010-11

= ₹ 8,31,000 – ₹ 5,52,000 = ₹ 2,79,000

Year 2013-14

Fair value of option per share = ₹ 15

Number of shares not subscribed = (554 – 550) × 100 = 400

Value of option forfeited = 400 × ₹ 15 = ₹ 6,000

Employees' Compensation A/c

Year		*₹*	*Year*		*₹*
2010-11	To ESOP Outstanding A/c	2,70,000	2010-11	By Profit & Loss A/c	2,70,000
		2,70,000			2,70,000
2011-12	To ESOP Outstanding A/c	2,82,000	2011-12	By Profit & Loss A/c	2,82,000
		2,82,000			2,82,000
2012-13	To ESOP Outstanding A/c	2,79,000	2012-13	By Profit & Loss A/c	2,79,000
		2,79,000			2,79,000

ESOP Outstanding A/c

Year		*₹*	*Year*		*₹*
2010-11	To Balance c/d	2,70,000	2010-11	By Employees' Compensation A/c	2,70,000
		2,70,000			2,70,000
2011-12	To Balance c/d	5,52,000	2011-12	By Balance b/d	2,70,000
				By Employees' Compensation A/c	2,82,000
		5,52,000			5,52,000
2012-13	To Balance c/d	8,31,000	2012-13	By Balance b/d	5,52,000
				By Employees' Compensation A/c	2,79,000
		8,31,000			8,31,000
2013-14	To General Reserve (400 × 15)	6,000	2013-14	By Balance b/d (55,400 × 15)	8,31,000
	To Share Capital (55,000 × 10)	5,50,000		By Bank (55,000 × 45)	24,75,000
	To Securities Premium (55,000 × 50)	27,50,000			
		33,06,000			33,06,000

Note: Securities Premium

	₹
Exercise price received per share	45
Value of service received per share	15
Consideration received per share	60
Less: Nominal value per share	(10)
Securities premium per share	50

Computation of Basic EPS

	2010-11 *₹ 000*	*2011-12* *₹ 000*	*2012-13* *₹ 000*
Profit before amortisation of ESOP costs	1,190	1,262	1,379
Less: ESOP cost amortised	(270)	(282)	(279)
Net profit for shareholders	920	980	1,100
Number of shares outstanding ('000)	400	400	400
Basic EPS	2.30	2.45	2.75

Potential Equity

	2010-11	*2011-12*	*2012-13*
A. Actual number of employees	585	565	554
B. Option granted per employee	100	100	100
C. Number of options outstanding	58,500	56,500	55,400
D. Unamortised ESOP cost per option (₹)	10*	5**	Nil
E. Exercise Price (₹ 45)	45	45	45
F. Expected exercise price to be received (C x E): ₹ 000	2,632.5	2,542.5	2,493.0
G. Unamortised ESOP cost (C × D) : ₹ 000	585.0	282.5	Nil
H. Total proceeds: ₹ 000	3,217.5	2,825.0	2,493.0
I. Fair value per share (₹)	60	66	72
J. Number of shares issued for consideration (H/I)	53,625	42,803	34,625
K. Potential Equity (C – J)	4,875	13,697	20,775

* [15-(15/3)] = 10

** [15-{(15/3) x 2}] = 5

Computation of Diluted EPS

	2010-11 ₹	2011-12 ₹	2012-13 ₹
Net profit for shareholders	9,20,000	9,80,000	11,00,000
Number of shares outstanding	4,00,000	4,00,000	4,00,000
Potential Equity	4,875	13,697	20,775
Total number of share	4,04,875	4,13,697	4,20,775
Diluted EPS	2.27	2.37	2.61

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On 1 April 20X7 Pauline acquired the following non-current investments:

- 6 million equity shares in Sonia by an exchange of two shares in Pauline for every four shares in Sonia plus $1.25 per acquired Sonia share in cash. The market price of each Pauline share at the date of acquisition was $6 and the market price of each Sonia share at the date of acquisition was $3.25.
- 30% of the equity shares of Arthur at a cost of $7.50 per share in cash.

Only the cash consideration of the above investments has been recorded by Pauline. In addition $1,000,000 of professional costs relating to the acquisition of Sonia is included in the cost of the investment.

The summarised draft statements of financial position of the three companies at 31 March 20X8 are presented below:

	Pauline	Sonia	Arthur
	$000	$000	$000
Assets			
Non-current assets			
Property, plant and equipment	36,800	20,800	36,000
Investments in Sonia and Arthur	26,500	–	–
Financial assets	13,000	–	–
	76,300	20,800	36,000
Current assets			
Inventories	13,800	12,400	7,200
Trade receivables	6,400	3,000	4,800
Total assets	96,500	36,200	48,000
Equity and liabilities			
Equity shares of $1 each	20,000	8,000	8,000
Retained earnings			
– at 31 March 20X7	32,000	12,000	22,000
– for year ended 31 March 20X8	18,500	5,800	10,000
	70,500	25,800	40,000
Non-current liabilities			
7% Loan notes	10,000	2,000	2,000
Current liabilities			
Trade payables	16,000	8,400	6,000
	96,500	36,200	48,000

The following information is relevant to the preparation of the consolidated statement of financial position:

(i) At the date of acquisition Sonia had an internally generated brand name. The directors of Pauline estimate that this brand name has a fair value of $2 million, an indefinite life and has not suffered any impairment.

(ii) On 1 April 20X7, Pauline sold an item of plant to Sonia at its agreed fair value of $5 million. Its carrying amount prior to the sale was $4 million. The estimated remaining life of the plant at the date of sale was five years.

(iii) During the year ended 31 March 20X8 Sonia sold goods to Pauline for $5.4 million. Sonia had marked up these goods by 50% on cost. Pauline had a third of the goods still in its inventory at 31 March 20X8. There were no intra-group payables or receivables at 31 March 20X8.

(iv) Pauline has a policy of valuing non-controlling interests at fair value at the date of acquisition. For this purpose the share price of Sonia at this date should be used. Impairment tests on 31 March 20X8 concluded that neither consolidated goodwill or the value of the investment in Arthur were impaired.

(v) The financial assets in Pauline's statement of financial position are classified as fair value through profit or loss. In the draft financial statements, they are held at their fair value on 1 April 20X7. They have a fair value of $18 million at 31 March 20X8.

(vi) No dividends were paid during the year by any of the companies.

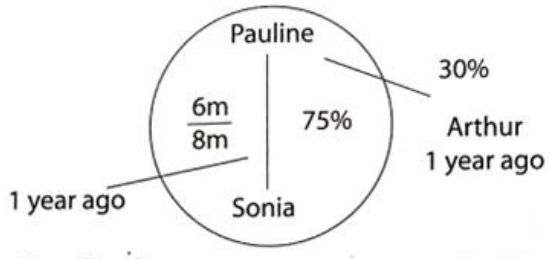
Required:

Prepare the consolidated statement of financial position for the Pauline group as at 31 March 20X8.

Solution:

Workings

(W1) **Group structure**



(W2) **Net assets – Sonia**

	At acquisition date
	$000
Equity capital	8,000
Retained earnings	12,000
Fair value adj:	
Brand	2,000
	22,000

Note: Post Acquisition Profits

Profit for the year	5,800
Less: PURP on inventories	600
	5,200

(W3) **Goodwill**

	Sonia
	$000
Fair value of consideration	
Share exchange (6m × 2/4 × $6)	18,000
Cash paid (6m × $1.25)	7,500
	25,500
FV of NCI at acquisition (2m × $3.25)	6,500
	32,000
Less FV of net assets at acquisition (W2)	(22,000)
	10,000

The 3 million shares issued by Pauline in the share exchange at a value of $6 each would be recorded as $1 per share in equity capital and $5 per share in share premium. This gives an increase in equity capital of $3 million and a share premium of $15 million.

(W4) **NCI**

	$000
Fair value of NCI at acquisition (W3)	6,500
NCI share of post-acquisition net asset movement (25% × 5200 (W2)	1,300
	7,800

(W5) **Group retained earnings**

	$000
100% of Pauline's retained earnings ($32,000 + $18,500)	50,500
Professional costs written off	(1,000)
Gain on financial assets (W9)	5,000
P% of Sonia's post-acquisition retained earnings** (75% × (($17,800 – $600) – $12,000) (W2))	3,900
P% of Arthur's post-acquisition retained earnings (30% × $10,000)	3,000
PPE PURP (W8)	(800)
	60,600

** It is worth noting that, if the subsidiary has no 'other components of equity', then you could simply take P's share of the subsidiary's post-acquisition net assets movement:

75% × (5200 (W2)) = $3,900.

(W6) **Investment in associate**

	$000
Cost (8,000 × 30% × $7.50)	18,000
P's share post-acquisition reserves ($10,000 × 30%)	3,000
	21,000

(W7) **PURP in inventory**

Intra-group sales are $5.4 million on which Sonia made a profit of $1,800,000 ($5,400,000 × 50/150).

The unrealised profit still in inventory is therefore $600,000 ($1,800,000 × 1/3).

Sonia is the seller so the profit must be removed from Sonia's retained earnings in W2.

The adjusting entry is:

Dr Retained earnings (W2)	$600,000
Cr Inventories	$600,000

(W8) **PURP in PPE**

The carrying value of the PPE is $4m ($5m – ($5m/5 years)).

If no group transfer had happened, then the carrying value would have been $3.2m ($4m – ($4m/5 years).

PPE must therefore be reduced by $800,000 ($4m – $3.2m). Pauline is the seller so the profit impact must be adjusted against Pauline's retained earnings in W5. The adjusting entry is:

Dr Retained earnings (W5)	$800,000
Cr PPE	$800,000

(W9) **Financial assets**

The financial assets must be remeasured to fair value and the gain recorded through profit or loss.

The gain on revaluation to fair value is $5m ($18m – $13m). This will be recorded in profit or loss and will increase group retained earnings in W5.

Solution

Consolidated statement of financial position as at 31 March 20X8

	$000
Assets	
Non-current assets	
Property, plant and equipment ($36,800 + $20,800 – $800 (W8))	56,800
Goodwill (W3)	10,000
Intangible assets (W2)	2,000
Investment in associate (W6)	21,000
Financial assets (W9)	18,000
	107,800
Current assets	
Inventories ($13,800 + $12,400 – $600 (W7))	25,600
Trade receivables ($6,400 + $3,000)	9,400
Total assets	142,800
Equity and liabilities	
Equity attributable to equity holders of the parent	
Equity shares of $1 each ($20,000 + $3,000 (W3))	23,000
Share premium (W3)	15,000
Retained earnings (W5)	60,600
	98,600
Non-controlling interest (W4)	7,800
Total equity	106,400
Non-current liabilities	
7% Loan notes ($10,000 + $2,000)	12,000
Current liabilities	
Trade payables ($16,000 + $8,400)	24,400
Total equity and liabilities	142,800