

CHAPTER 23**CONSOLIDATED AND SEPARATE FINANCIAL STATEMENTS OF GROUP ENTITIES****UNIT 3: IND AS 28 INVESTMENTS IN ASSOCIATES AND JV****PRACTICE QUESTIONS****QUESTION FROM ICAI STUDY MATERIAL****Accounting entries related investment in associate / joint venture**

Q1: On the first day of a financial year, A Ltd. invested in the equity share capital of B Ltd. at a cost of ₹ 1,00,000 to acquire 25% share in the voting power of B Ltd. A Ltd. has concluded that B Ltd. is an associate of A Ltd. At the end of the year, B Ltd. earned profit of ₹ 10,000 and other comprehensive income of ₹ 2,000. In that year, B Ltd. also declared dividend to the extent of ₹ 4,000. Pass necessary entries in the books of A Ltd. to account for the investment in associate.

[MTP May 2023]

Ans: Following entries would be passed in the books of A Ltd.:

- 1) Initial entry to record investment done in associate

Investment in B Ltd. A/c	Dr.	1,00,000
To Bank A/c		1,00,000

- 2) Recording of share in the profit of the associate

Investment in B Ltd. A/c	Dr.	2,500
To Share in profit of investee (P&L)		2,500

[A Ltd. share in profit would be ₹ 2,500 (₹ 10,000 x 25%)]

- 3) Recording of share in the other comprehensive income (OCI) of the associate

Investment in B Ltd. A/c	Dr.	500
To Share in OCI of investee (OCI)		500

[A Ltd. share in OCI would be ₹ 500 (₹ 2,000 x 25%)]

- 4) Recording of dividend distributed by associate

Dividend Receivable A/c	Dr	1,000
To Investment in B Ltd. A/c		1,000

[A Ltd. share in dividend would be ₹ 1,000 (₹ 4,000 x 25%)]

Q2: B Ltd acquired a 30% interest in D Ltd and achieved significant influence. The cost of the investment was ₹ 2,50,000. The associate has net assets of ₹ 5,00,000 at the date of acquisition. The fair value of those net assets is ₹ 6,00,000 as a fair value of property, plant & equipment is ₹ 1,00,000 higher than its book value. This property, plant & equipment has a remaining useful life of 10 years.

After acquisition D Ltd recognize profit after tax of ₹ 1,00,000 and paid a dividend out of these profits of ₹ 9,000. D Ltd has also recognized exchange losses of ₹ 20,000 directly in other comprehensive income. Calculate B Ltd's interest in D Ltd at the end the year by using equity method.

Ans:

B Ltd's interest in D Ltd at the end the year is calculated as follows:	₹
Balance on requisition under the equity method (including goodwill of ₹ 70,000)	
(₹ 2,50,000 – (30% X ₹ 6,00,000))	2,50,000
B Ltd's share of D Ltd's after tax profit (30% X ₹1,00,000)	30,000
Elimination of dividend received by B Ltd from D Ltd (30% X ₹9,000)	(2,700)
B Ltd's share of D Ltd's exchange differences (30% X ₹20,000)	(6,000)
B Ltd's share of amortisation of fair value uplift (30% X ₹10,000)	(3,000)
B Ltd's interest in D Ltd at the end of the year under the equity method (including goodwill)	2,68,300

D Ltd has net assets at the end of the year of ₹ 5,71,000 (that is, net assets at the start of the year of ₹ 5,00,000 , plus profit during the year of ₹ 1,00,000 , less dividend of ₹ 9,000 , less foreign exchange losses of ₹ 20,000).

B Ltd's interest in D Ltd at the end of the year is made up of:

B Ltd's share of D Ltd's net assets (30% X ₹5,71,000)	1,71,300
Goodwill	70,000
B Ltd's share of D Ltd's fair value adjustments (the initial fair value difference of ₹1,00,000 has been reduced by ₹10,000 due to depreciation in the year)	
(30% X ₹90,000)	27,000
B Ltd's interest in D Ltd	2,68,300

Exemption from applying equity method

Q3: MNO Ltd. holds 15% of the voting power of DEF Ltd. PQR Mutual Fund (which is a subsidiary of MNO Ltd.) also holds 10% voting power of DEF Ltd. Hence, MNO Ltd. holds total 25% voting power of DEF Ltd. (15% held by own and 10% held by subsidiary) and accordingly has significant influence over DEF Ltd. How should MNO Ltd. account for investment in DEF Ltd. in its consolidated financial statements?

Ans: The 15% interest which is held directly by MNO Ltd. should be measured as per equity method of accounting. However, with respect to the 10% interest which is held through a mutual fund,

MNO Ltd. can avail the exemption from applying the equity method to that 10% interest and instead measure that investment at fair value through profit or loss. To summarise, the total interest of 25% in DEF Ltd. should be measured as follows:

- 15% interest held directly by MNO Ltd.: Measure as per equity method of accounting
- 10% interest held indirectly through a mutual fund: Measure as per equity method of accounting or at fair value thorough profit or loss as per Ind AS 109

Acquisition of interest in an associate

Q4: Blue Ltd. acquired 25% of the equity share capital of Green Ltd. on the first day of the financial year for ₹1,25,000. As of that date, the carrying value of the net assets of Green Ltd. was ₹3,00,000 and the fair value was ₹ 4,00,000. The excess of fair value over the carrying value was attributable to one of the buildings owned by Green Ltd. having a remaining useful life of 20 years. Green Ltd. earned profit of ₹ 40,000 and other comprehensive income of ₹ 10,000 during the year. Calculate the goodwill / capital reserve on the date of acquisition, Blue Ltd.'s share in the profit and other comprehensive income for the year and closing balance of investment at the end of the year. [MTP NOV 2021]

Ans:

1. Goodwill / capital reserve on the date of acquisition

The cost of the investment is higher than the net fair value of the investee's identifiable assets and liabilities. Hence there is goodwill. Amount of goodwill is calculated as follows

	₹
Cost of acquisition of investment	1,25,000
Blue Ltd.'s share in fair value of net assets of Green Ltd. on the date of acquisition (4,00,000 * 25%)	<u>(1,00,000)</u>
Goodwill	<u>25,000</u>

Above goodwill will be recorded as part of carrying amount of the investment.

2. Share in profit and other comprehensive income of Gren Ltd.

	₹
Share in profit of Green Ltd. (40,000 x 25%)	10,000
Adjustment for depreciation based on fair value (1,00,000 ÷ 20) x 25%	(1,250)
Share in profit after adjustment	8,750
Share in other comprehensive income (10,000 x 25%)	2,500

3. Closing balance of investment at the end of the year

	₹

Cost of acquisition of investment (including goodwill of ₹ 25,000)	1,25,000
Share in profit after adjustments	8,750
Share in other comprehensive income	<u>2,500</u>
Closing balance of investment	<u>1,36,250</u>

Q5: On 1st April 2019, Investor Ltd. acquires 35% interest in another entity, XYZ Ltd. Investor Ltd. determines that it is able to exercise significant influence over XYZ Ltd. Investor Ltd. has paid total consideration of ₹ 47,50,000 for acquisition of its interest in XYZ Ltd. At the date of acquisition, the book value of XYZ Ltd.'s net assets was ₹ 90,00,000 and their fair value was ₹ 1,10,00,000. Investor Ltd. has determined that the difference of ₹ 20,00,000 pertains to an item of property, plant and equipment (PPE) which has remaining useful life of 10 years.

During the year, XYZ Ltd. made a profit of ₹ 8,00,000. XYZ Ltd. paid a dividend of ₹ 12,00,000 on 31st March, 2020. XYZ Ltd. also holds a long-term investment in equity securities. Under Ind AS, investment is classified as at FVTOCI in accordance with Ind AS 109 and XYZ Ltd. recognized an increase in value of investment by ₹ 2,00,000 in OCI during the year. Ignore deferred tax implications, if any.

Calculate the closing balance of Investor Ltd.'s investment in XYZ Ltd. as at 31st March, 2020 as per the relevant Ind AS. **[RTP Nov 20; MTP Nov 22; May 2024; Exam Nov 22 (5 Marks)]**

Ans: Calculation of Investor Ltd.'s investment in XYZ Ltd. under equity method:

	₹	₹
Acquisition of investment in XYZ Ltd.		
Share in book value of XYZ Ltd.'s net assets (35% of ₹90,00,000)	31,50,000	
Share in fair valuation of XYZ Ltd.'s net assets [35% of (₹ 1,10,00,000 – ₹90,00,000)]	7,00,000	
Goodwill on investment in XYZ Ltd. (balancing figure)	<u>9,00,000</u>	
Cost of investment		47,50,000
Profit during the year		
Share in the profit reported by XYZ Ltd. (35% of ₹8,00,000)	2,80,000	
Adjustment to reflect effect of fair valuation [35% of (₹20,00,000/10 years)]	<u>(70,000)</u>	
Share of profit in XYZ Ltd. 4recognized in income by Investor Ltd.		2,10,000
Long term equity investment		
FVTOCI gain recognized in OCI (35% of ₹ 2,00,000)		70,000
Dividend received by Investor Ltd. during the year [35% of ₹12,00,000]		<u>(4,20,000)</u>
Closing balance of Investor Ltd.'s investment in XYZ Ltd.		<u>46,10,000</u>

Cumulative preference shares issued by associate or joint venture

Q6: KL Ltd. has invested in 50% voting power of a joint venture MN Ltd. MN Ltd. has also issued 10% cumulative preference shares to other investors worth ₹ 10,00,000. During the year, MN Ltd. earned profit of ₹ 4,00,000. Also, MN Ltd. has not declared any dividend on the preference shares for current year. Calculate KL Ltd.'s share in the net profit of MN Ltd. for the year.

Ans: If an associate or a joint venture has outstanding cumulative preference shares that are held by parties other than the entity and are classified as equity, the entity should compute its share of profit or loss after adjusting for dividend on such shares, whether or not the dividends have been declared.

In current case, KL Ltd.'s share in net profit of MN Ltd. would be as follows.

	₹
Profit of MN Ltd. for the year	4,00,000
Dividend on cumulative preference shares (10,00,000*10%)	<u>(1,00,000)</u>
Net profit attributable to the holders of equity share	<u>3,00,000</u>
KL Ltd.'s 50% share in net profit of MN Ltd.	1,50,000

Q7: Entity A holds a 20% equity interest in Entity B (an associate) that in turn has a 100% equity interest in Entity C. Entity B recognised net assets relating to Entity C of ₹ 1,000 in its consolidated financial statements. Entity B sells 20% of its interest in Entity C to a third party (a non-controlling shareholder) for ₹ 300 and recognises this transaction as an equity transaction in accordance with paragraph 23 of Ind AS 110, resulting in a credit in Entity B's equity of ₹ 100.

The financial statements of Entity A and Entity B are summarised as follows before and after the transaction:

Before**A's consolidated financial statements**

Assets	₹	Liabilities	₹
Investment in B	200	Equity	200
Total	200	Total	200

B's consolidated financial statements

Assets	₹	Liabilities	₹
Assets (from C)	1000	Equity	1000
Total	1000	Total	1000

The financial statements of B after the transaction are summarised below:

After**B's consolidated financial statements**

Assets	₹	Liabilities	₹
Assets (from C)	1000	Equity	1000
Cash	300	Equity transaction with non- controlling interest	100
		Equity attributable to owners	1100
		Non-controlling interest	200
Total	1300	Total	1300

Although Entity A did not participate in the transaction, Entity A's share of net assets in Entity B increased as a result of the sale of B's 20% interest in C. Effectively, A's share in B's net assets is now ₹ 220 (20% of ₹ 1,100) i.e., ₹ 20 in addition to its previous share.

How is an equity transaction that is recognised in the financial statements of Entity B reflected in the consolidated financial statements of Entity A that uses the equity method to account for its investment in Entity B?

Ans: Ind AS 28 defines the equity method as “a method of accounting whereby the investment is initially recognised at cost and adjusted thereafter for the post-acquisition change in the investor's share of the investee's net assets. The investor's profit or loss includes its share of the investee's profit or loss and the investor's other comprehensive income includes its share of the investee's other comprehensive income.”

Paragraph 27 of Ind AS 28, states, inter alia, that when an associate or joint venture has subsidiaries, associates or joint ventures, the profit or loss, other comprehensive income, and net assets taken into account in applying the equity method are those recognised in the associate's or joint venture's financial statements (including the associate's or joint venture's share of the profit or loss, other comprehensive income and net assets of its associates and joint ventures), after any adjustments necessary to give effect to uniform accounting policies.

The change of interest in the net assets / equity of the associate as a result of the investee's equity transaction is reflected in the investor's financial statements as 'share of other changes in equity of investee' (in the statement of changes in equity) instead of gain in Statement of profit and loss, since it reflects the post-acquisition change in the net assets of the investee as per paragraph 3 of Ind AS 28 and also faithfully reflects the investor's share of the associate's transaction as presented in the associate's consolidated financial statements.

Thus, in the given case, Entity A recognises ₹ 20 as change in other equity instead of in statement of profit and loss and maintains the same classification as of its associate, Entity B, i.e., a direct credit to equity as in its consolidated financial statements.

Upstream and downstream transaction between an entity and its associate

Q8: Scenario A M Ltd. has invested in 40% share capital of N Ltd. and hence N Ltd. is an associate of M Ltd. During the year, N Ltd. sold inventory to M Ltd. for a value of ₹ 10,00,000. This included profit of 10% on the transaction price i.e. profit of ₹ 1,00,000. Out the above inventory, M Ltd. sold inventory of ₹ 6,00,000 to outside customers. Hence, the inventory of ₹ 4,00,000 purchased

from N Ltd. is still lying with M Ltd. Determine the unrealised profit to be eliminated on above transaction.

Scenario B Assume the same facts as per Scenario A except that the inventory is sold by M Ltd. to N Ltd. instead of N Ltd. selling to M Ltd. Determine the unrealised profit to be eliminated on above transaction.

Ans: **Scenario A** Firstly, as part of its equity method accounting for investment in N Ltd., M Ltd. will pass this journal entry:

Investment in N Ltd.	Dr. 40,000
To Share in profit of N Ltd.	40,000

Out of the inventory of ₹ 10,00,000, M Ltd. has sold inventory worth ₹ 6,00,000 to outside customers. Hence, the profit of ₹ 60,000 ($6,00,000 \times 10\%$ profit margin) on such inventory is realised. However, the inventory worth ₹ 4,00,000 is still held by M Ltd. which consists profit of ₹ 40,000 ($4,00,000 \times 10\%$). Hence, M Ltd.'s share in such profit i.e., ₹ 16,000 ($40,000 \times 40\%$) is considered as unrealised.

Accordingly, after recording of share in total profit of N Ltd., M Ltd. should pass following adjustment entry to reverse the unrealised profit margin:

Share in profit of N Ltd.	Dr. 16,000
To Inventory	16,000

In subsequent period, when this inventory of ₹ 4,00,000 is sold by N Ltd. to an outside customer then the above profit margin of ₹ 16,000 will be treated as realised and hence the above entry will be reversed in that period.

Note: in the separate financial statements of M Ltd., inventory is carried at ₹ 4,00,000 whereas in its consolidated financial statements, inventory is carried at ₹ 3,84,000 (due to elimination entry above in respect of unrealized profit). In the subsequent period, when the inventory is sold, Inventory Account is credited by ₹ 4,00,000 whereas for the purpose of consolidated financial statements, it should have been credited by only ₹ 3,84,000. The difference is adjusted by debiting back ₹ 16,000 to the Inventory Account and a corresponding recognition of share in profit of associate.]

Scenario B Out of the inventory of ₹ 10,00,000, N Ltd. has sold inventory worth ₹ 6,00,000 to outside customers. Hence, the profit of ₹ 60,000 ($6,00,000 \times 10\%$ profit margin) on such inventory is realised. However, the inventory worth ₹ 4,00,000 is still held by N Ltd. which consists profit of ₹ 40,000 ($4,00,000 \times 10\%$). Out of this profit of ₹ 40,000, profit to the extent of other investor's interest in the investee is treated as realised profit i.e. ₹ 24,000 ($40,000 \times 60\%$) is treated as realised profit. Balance profit of ₹ 16,000 ($40,000 \times 40\%$) is considered as unrealised. Hence, M Ltd. should pass following adjustment entry to reverse the unrealised profit:

Sales	Dr. 160,000
To Cost of material consumed	144,000
To Investment in N Ltd.	16,000

In subsequent period, when this inventory of ₹ 4,00,000 is sold by N Ltd. to an outside customer then the above profit margin of ₹ 16,000 will be treated as realised and hence the above entry will be reversed in that period.

Impairment loss on downstream and upstream transaction between an entity and its joint venture

Q9: Scenario A: X Ltd. has invested in a joint venture Y Ltd. by holding 50% of its equity share capital. During the year, X Ltd. sold an asset to Y Ltd. at its market value of ₹ 8,00,000. The asset's carrying value in X Ltd.'s books was ₹ 10,00,000. Determine how should X Ltd. account for the sale transaction in its books.

Scenario B Assume the same facts as per Scenario A except that the asset is sold by Y Ltd. to X Ltd. instead of X Ltd. selling to Y Ltd. Determine how should X Ltd. account for the above transaction in its books. **[MTP Nov 2023]**

Ans: Scenario A X Ltd. should record full loss of ₹ 2,00,000 (10,00,000 – 8,00,000) in its books as that would represent the impairment loss because the market value has actually declined. This loss would have been recorded even if X Ltd. would have first impaired the asset and then sold to Y Ltd. at zero profit / loss. Following entry should be passed in the books of X Ltd.

Bank A/c	Dr.	8,00,000	
Loss on sale of asset	Dr.	2,00,000	
To Asset			10,00,000

Scenario B X Ltd. should record loss to the extent of its share in Y Ltd. Hence, X Ltd.'s share in loss i.e. ₹ 1,00,000 [(10,00,000 – 8,00,000) x 50%] should be recorded by X Ltd. in its books. The loss should be recorded since the market value of the asset has actually declined and this would represent impairment. This loss would have been recorded even if Y Ltd. would have first recorded an impairment loss of ₹ 2,00,000 and then sold to X Ltd. at zero profit / loss. Following entry should be passed in the books of X Ltd.

Asset	Dr.	8,00,000	
Share in loss of Y Ltd.	Dr.	1,00,000	
To Bank			8,00,000
To Investment in Y Ltd.			1,00,000

Loss making associate and long-term interests

Q10: An entity has following three type interests in an associate:

- Equity shares: 25% of the equity shares to which equity method of accounting is applied
- Preference shares: Non-cumulative preference shares that form part of net investment in the associate. Such preference shares are measured at fair value as per Ind AS 109.

- c) Long-term loan: The loan carrying interest of 10% p.a. The interest income is received at the end of each year. The long-term loan is accounted as per amortised cost as per Ind AS 109. This loan also forms part of net investment in the associate.

At the start of year 1, the carrying value of each of the above interests is as follows:

- Equity shares – ₹ 10,00,000
- Preference shares – ₹ 5,00,000
- Long-term loan – ₹ 3,00,000

Following table summarises the changes in the fair value of preference shares as per Ind AS 109, impairment loss on long-term loan as per Ind AS 109 and entity's share in profit / loss of associate for year 1-5.

End of Year	Increase / (Decrease) in fair value of preference shares as per Ind AS 109	Impairment loss / (reversal) on long-term loan as per Ind AS 109	Entity's share in profit / (loss) of associate
1	(50,000)	(50,000)	(16,00,000)
2	(50,000)	-	(2,00,000)
3	1,00,000	50,000	-
4	50,000	-	10,00,000
5	30,000	-	10,00,000

Throughout year 1 to 5, there has been no objective evidence of impairment in the net investment in the associate. The entity does not have any legal or constructive obligation to share the losses of the associate beyond its interest in the associate.

Based on above, determine the closing balance of each of the above interests at the end of each year.

Ans: Year 1 Below table summarises the closing balance of each of the interest at the end of year 1:

Type of interest	Opening balance at the start of the year	Adjustment as per Ind AS 109	Balance after applying Ind AS 109	Share in profit / (loss) of associate	Closing balance at the end of the year
	(A)	(B)	I = (A+B)	(D)	I = (C+D)
Equity shares	10,00,000	NA	10,00,000	(10,00,000)	-
Preference shares	5,00,000	(50,000)	4,50,000	(4,50,000)	-
Long-term loan	3,00,000	(50,000)	2,50,000	(1,50,000)	1,00,000
Total	18,00,000	(1,00,000)	17,00,000	(16,00,000)	1,00,000

The entire loss of ₹ 16,00,000 is recognised. Hence, there is no unrecognised loss at the end of year 1.

Year 2 Below table summarises the closing balance of each of the interest at the end of year 2:

Type of interest	Opening balance at the start of the year	Adjustment as per Ind AS 109	Balance after applying Ind AS 109	Share in profit / (loss) of associate	Closing balance at the end of the year
	(A)	(B)	I = (A+B)	(D)	I = (C+D)
Equity shares	-	NA	-	-	-
Preference shares	-	(50,000)	(50,000)	50,000 *	-
Long-term loan	<u>1,00,000</u>	<u>-</u>	<u>1,00,000</u>	<u>(1,00,000)</u>	<u>-</u>
Total	<u>1,00,000</u>	<u>(1,00,000)</u>	<u>17,00,000</u>	<u>(50,000)</u>	<u>-</u>

* Recognition of changes in fair value as per Ind AS 109 has resulted in the carrying amount of Preference shares being negative ₹ 50,000. Consequently, the entity shall reverse a portion of the associate's losses previously allocated to Preference shares.

Out of the total loss of ₹ 2,00,000 for the year, loss of only ₹ 50,000 is recognized. Hence, there is unrecognized loss to the extent of ₹ 1,50,000 at the end of year 2.

Year 3 Below table summarises the closing balance of each of the interest at the end of year 3: ₹

Type of interest	Opening balance at the start of the year	Adjustment as per Ind AS 109	Balance after applying Ind AS 109	Share in profit / (loss) of associate	Closing balance at the end of the year
	(A)	(B)	I = (A+B)	(D)	I = (C+D)
Equity shares	-	NA	-	-	-
Preference shares	-	1,00,000	1,00,000	(1,00,000)	-
Long-term loan	<u>-</u>	<u>50,000</u>	<u>50,000</u>	<u>(50,000)</u>	<u>-</u>
Total	<u>-</u>	<u>1,50,000</u>	<u>1,50,000</u>	<u>(1,50,000)</u>	<u>-</u>

The share in profit / loss for the year is nil. However, there was previously unrecognised loss of ₹ 1,50,000 which is allocated in current year. After recognising the above loss, there is no unrecognised loss at the end of year 3.

Year 4 Below table summarises the closing balance of each of the interest at the end of year 4:

Type of interest	Opening balance at the start of the year	Adjustment as per Ind AS 109	Balance after applying Ind AS 109	Share in profit / (loss) of associate	Closing balance at the end of the year
	(A)	(B)	I = (A+B)	(D)	I = (C+D)
Equity shares	-	NA	-	2,00,000	2,00,000
Preference shares	-	50,000	50,000	5,00,000	5,50,000
Long-term loan	<u>-</u>	<u>-</u>	<u>-</u>	<u>3,00,000</u>	<u>3,00,000</u>

Total	_____ -	<u>50,000</u>	<u>50,000</u>	<u>10,00,000</u>	<u>10,50,000</u>
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The entity's share in profit of associate for the year is ₹ 10,00,000. The entity shall allocate such profit to each of the instruments in order of their seniority in liquidation. The entity should limit the amount of profit to be allocated to preference shares and long-term loan to the extent of losses previously allocated to them. Hence, the entity has allocated ₹ 5,00,000 to preference shares and ₹ 3,00,000 to long-term debt.

There is no unrecognised loss at the end of year 4.

Year 5 Below table summarises the closing balance of each of the interest at the end of year 5:

Type of interest	Opening balance at the start of the year	Adjustment as per Ind AS 109	Balance after applying Ind AS 109	Share in profit / (loss) of associate	Closing balance at the end of the year
	(A)	(B)	I = (A+B)	(D)	I = (C+D)
Equity shares	2,00,000	NA	2,00,000	10,00,000	12,00,000
Preference shares	5,50,000	30,000	5,80,000	-	5,80,000
Long-term loan	<u>3,00,000</u>	<u>_____ -</u>	<u>3,00,000</u>	<u>_____ -</u>	<u>3,00,000</u>
Total	<u>10,50,000</u>	<u>30,000</u>	<u>10,80,000</u>	<u>10,00,000</u>	<u>20,80,000</u>

The entity's share in profit of associate for the year is ₹ 10,00,000. The entire profit is allocated to equity shares since there is no loss previously allocated to either preference shares or long-term loan.

There is no recognized loss at the end of year 5.

Year 1 to 5 The interest accrual on long-term loan would be done in each year at 10% p.a. This will be done without taking into account any adjustment done in the carrying value of long-term loan as per Ind AS 28. Hence, the entity will accrue interest of ₹ 30,000 (3,00,000 x 10%) in each year.

Recording in profit or loss of the gain / loss on discontinuation of equity method

Q11: CD Ltd. held 50% of the voting power of RS Ltd. which is a joint venture of CD Ltd. The carrying value of the investment in RS Ltd. is ₹ 1,00,000. Now out of the 50% stake, CD Ltd. has sold 20% stake in RS Ltd. to a third party for a consideration of ₹ 80,000. The fair value of the retained 30% interest is ₹ 1,20,000. Determine how much gain / loss should be recorded in profit or loss of CD Ltd.

Ans: CD Ltd. Shall record in profit or loss difference between below:

- the fair value of any retained interest (i.e. ₹ 1,20,000) and any proceeds from disposing of a part interest in the joint venture (i.e. ₹ 80,000); and
- the carrying amount of the investment at the date the equity method was discontinued (i.e. 1,00,000).

Hence, CD Ltd. Shall record gain of ₹ 1,00,000 in profit or loss.

Investment in joint venture held for sale

Q12: Ram Ltd. holds 50% of the equity share capital of Shyam Ltd. The balance 50% equity share capital is held by another investor. Ram Ltd. has joint control over Shyam Ltd. and it is a joint venture of Ram Ltd., accounted using equity method. Now Ram Ltd. is planning to sell 10% of the equity share capital of Shyam Ltd. to a third party. Such 10% investment meets the criteria of an asset held for sale and has been measured and disclosed accordingly. Now determine how should Ram Ltd. account 40% interest retained in Shyam Ltd.

Ans: Till the time 10% stake is sold, Ram Ltd. shall account for the retained interest of 40% as per equity method. After the sale of 10% investment, if Ram Ltd. still has joint control over Shyam Ltd. (e.g. through contractual arrangement) then it shall continue to measure that investment using equity method. However, if Ram Ltd. is not going to have joint control over Shyam Ltd. post the disposal of 10% investment then retained investment of 40% shall be accounted as per Ind AS 109.

Q13: M Limited holds 90% interest in subsidiary N Limited. N Limited holds 25% interest in an associate O Limited. As at 31 March 20X1, the net assets of O Limited was ₹ 300 lakhs including profit of ₹ 40 lakhs for the year ended 31 March 20X1. Calculate how the investment in O Limited will be accounted in the consolidated financial statements of M Limited?

Ans: Since N Limited is a subsidiary of M Limited, the consolidated financial statements of M Limited will include 100% amounts of the consolidated financial statements of N Limited (including investment in O Limited accounted for using equity method). Accordingly, the investment in O Limited will be accounted as follows in the consolidated financial statements of M Limited:

	₹' lakh	
Investment in O Limited (300 x 25%)		75
Share in profit of O Limited		
Attributable to M Limited (40 x 25% x 90%)	9	
Attributable to Non-controlling interest of N Limited (40 x 25% x 10%)	1	10

Q14: AB Limited holds 30% interest in an associate which it has acquired for a cost of ₹ 300 lakhs. On the date of acquisition of that stake, the fair value of net assets of the associate was ₹ 900 lakh. The value of goodwill on acquisition was ₹ 30 lakhs. After the acquisition, AB Limited accounted for the investment in the associate as per equity method of accounting and now the carrying value of such investment in the consolidated financial statements of AB Limited is ₹ 360 lakhs. The associate has now issued equity shares to some investors other than AB Limited for a consideration of ₹ 800 lakhs. This has effectively reduced the holding of AB Limited to 20%. Determine how AB Limited should account for such reduction in interest in the associate?

Ans: Because of the issue of shares by associate to other investors, AB Limited has effectively sold 10% (30 – 20) of its interest in the associate. The gain / loss on reduction in interest in associate is calculated as follows:

	₹' lakhs
AB Limited's share in the consideration received by the associate for issue of shares (800 x 20%) (1)	160
Less: Carrying value of interest sold (360 x 1/3)(2)	(120)
Gain on reduction in interest in associate(3)	40

Notes:

- The share in the consideration received by associate on issue of shares (i.e. ₹ 160 lakhs) would be recorded as part of investment in associate.
- The carrying amount of interest sold (i.e. ₹ 120 lakhs) will be derecognised, including proportionate goodwill of ₹ 10 lakhs (30 * 1/3).
- Gain of ₹ 40 lakhs will be recorded in the profit or loss.

QUESTIONS FROM OTHER SOURCES

Q15: P Ltd. owns 80% of S and 40% of A. A is an associate. Balance Sheet of three companies as on 31.03.09 are: (₹ in lakhs)

	P Ltd.	S	A
Investment in S	800	-	-
Investment in A	600	-	-
Property, plant and equipment	1600	800	1000
Current assets	2200	3300	3650
Total	5200	4100	4650
Liabilities:			
Share capital Re. 1			
Equity share	1000	400	800
Retained earnings	4000	3400	3600
Creditors	200	300	250
Total	5200	4100	4650

- P Ltd. acquired shares in 'S' many years ago when 'S' retained earnings were ₹ 520 lakhs.
- P Ltd. acquired its shares in 'A' on 01.04.08 when 'A' retained earnings were ₹ 400 lakhs.
- During the year, P Ltd sold goods to A for 10 lacs at a mark up of 25%. At year end, A Ltd. still holds one quarter of these goods in inventory.
- As a result of trading, P Ltd was owed ₹ 2,50,000 by A at reporting date. This agrees with the amount included in A Ltd's Trade receivables.

5. At year end it was determined that the investment in the associates was impaired by ₹ 35 lacs.
6. NCI are valued using the fair value method. The fair value of NCI at the date of acquisition was ₹ 200 lacs.

Prepare the Consolidated Balance Sheet of P Ltd.

[For Answer – Refer Class Notes]

Q16: Bright Ltd. acquired 30% of East India Ltd. shares for ₹ 2,00,000 on 01-04-20X1. By such an acquisition Bright can exercise significant influence over East India Ltd. During the financial year ending on 31-03-20X1 East India earned profits ₹ 80,000 and declared a dividend of ₹50,000 on 12-08-20X1. East India reported earnings of ₹3,00,000 for the financial year ending on 31-03-20X2 and declared dividends of ₹ 60,000 on 12-06-20X2.

Calculate the carrying amount of investment in:

- (i) Separate financial statements of Bright Ltd. as on 31-03-20X2;
- (ii) Consolidated financial statements of Bright Ltd.; as on 31-03-20X2;
- (iii) What will be the carrying amount as on 30-06-20X2 in consolidated financial statements?

Ans: Carrying amount of investment in Separate financial statements of Bright Ltd. as on 31-03-20X2:

	₹
Cost of Investment	2,00,000
Less: Dividend Received (credited to PL as per IND AS 27)	-
Carrying value as per Cost method	2,00,000

Carrying amount of investment in Consolidated financial statements of Bright Ltd. as on 31-03-20X2 as per equity method

	₹
Cost of Investment	2,00,000
Add: Share in Post-Acquisition Profit (3,00,000 x 30%)	90,000
Less: Dividend Received (50,000 x 30%)	(15,000)
Carrying value as per Equity method as on 31-03-20X2	2,75,000

Carrying amount of investment in Consolidated financial statements of Bright Ltd. as on 30-06-20X2 as per equity method

	₹
Carrying value of Investment as on 01-04-20X2	2,75,000
Less: Dividend Received (60,000 x 30%)	(18,000)
Carrying value as per Equity method as on 30-06-20X2	2,57,000

Q17: Eagle Ltd. had acquired 51% in Sparrow Ltd. for ₹ 75.80 lakhs on April 1st, 2010. On date of the acquisition Sparrow's Assets stood at ₹ 196 lakhs and liabilities at ₹ 16 lakhs. The Net asset

position of Sparrow Ltd. as on 31st March, 2011 & 30th September 2011 were ₹ 280 lakhs & ₹ 395 lakhs respectively, the increase resulting from profits earned during the period.

On 1st Oct, 2011, 25.5% holdings were sold for ₹ 125 lakhs. You are required to explain the nature of the relationship between the two companies on the relevant dates and the accounting adjustments that are necessary as a result of any change in the relationship. The profit arising on part sale of investment, carrying value of the portion unsold & goodwill/capital reserve that arises on change in nature of the investment may also be worked out by you.

Ans: Sparrow Ltd. became a subsidiary of Eagle Ltd. on 1st April 2010 when 51% thereof was acquired. The holding–subsidiary relationship continued till 30th September 2011 and from 1st October, 2011 the relationship between the two companies will change to Associate.

Ascertainment of Gain or Loss on the Disposal of the Part of the Investment in Sparrow Ltd.

		₹
Fair Value of consideration received on sale of 25.5% holdings in Sparrow Ltd.		1,25,00,000
Fair Value of Investment retained as Associate 25.5% holdings in Sparrow Ltd. (assumed proportionate to fair value of investment sold)		1,25,00,000
		2,50,00,000
Less: Net Assets of sparrow Ltd. on the date of disposal	3,95,00,000	
Share of Eagle Ltd. in Net Assets	2,01,45,000	
Less: Capital reserve on acquisition (Refer W.N.)	(16,00,000)	
Total value of investment in consolidated financial statements of Eagle Ltd.		1,85,45,000
Gain on loss of Control		64,55,000

Goodwill / Capital Reserve arising on the application of Equity Method on the date investee become an associate	₹
Fair Value of 25.5% holdings in Sparrow Ltd. as on 1 st October, 2011 – Deemed cost	1,25,00,000
Less: Share in Fair value of INA of Sparrow Ltd., as at date of investment when subsidiary relationship is transformed to an associate (3,95,00,000x 25.5%)	(1,00,72,500)
Goodwill arising on such investment under Equity method as per IND AS 28	(24,27,500)

Working Note:

Calculation of Goodwill / Gain on Bargain Purchase on the Date of Acquisition of Shares in Sparrow Ltd.

	₹
Net Assets on Acquisition date (₹ 1,96,00,000 – ₹ 16,00,000)	1,80,00,000
51% thereof	91,80,000
Less: Cost of investment	(75,80,000)
Gain on Bargain Purchase transferred to Capital Reserve on acquisition of Subsidiary	16,00,000

QUESTIONS FROM RTP/MTP/EXAMS/GFRS

Q18: Sumeru Limited holds 35% of total equity shares of Meru Limited, an associate company. The value of Investments in Meru Limited on March 31, 2018 is ₹ 3 crores in the consolidated financial statements of Sumeru Limited.

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

During the year ended March 31, 2019 the profit and loss statement of Meru Limited showed a loss of ₹ 1 crore.

- (A) What is the value of investment in Meru Limited as on March 31, 2019 in the consolidated financial statements of Sumeru Limited, if equity method is adopted for valuing the investments in associates?
- (B) Will your answer be different if Meru Limited had earned a profit of ₹ 1.50 crores and declared a dividend of ₹ 75 lakhs to the equity shareholders of the Company? **[GFRS]**

Ans: (a) Value of investment in Meru Ltd. as on 31st March, 2019 as per equity method in the consolidated financial statements of Sumeru Ltd.

	₹
Cost of Investment	3,00,00,000
Less: Share in Post-Acquisition Loss (1,00,00,000 x 35%)	(35,00,000)
Less: Unrealised gain on inventory left unsold with Meru Ltd.	
[{(50,000/3,00,000) x 1,00,000} x 35%]	<u>(5,833)</u>
Carrying value as per Equity method	<u>2,64,94,167</u>

(b) Value of investment in Meru Ltd. as on 31st March, 2019 as per equity method in the consolidated financial statements of Sumeru Ltd.

	₹
Cost of Investment	3,00,00,000
Add: Share in Post-Acquisition Profit (1,50,00,000 x 35%)	52,50,000
Less: Unrealised gain on inventory left unsold with Meru Ltd.	
[{(50,000/3,00,000) x 1,00,000} x 35%]	(5,833)
Less: Dividend (75,00,000 x 35%)	<u>(26,25,000)</u>
Carrying value as per Equity method	<u>3,26,19,167</u>

Note: In the absence of clarity in the information that whether unsold inventory is the cost value for Sumeru or Meru Ltd., the above solution has been given considering that ₹1,00,000 is the cost price of the inventory for Sumeru Ltd.

Alternatively, if it is considered as cost price to Meru Ltd. then the solution will be as follows:

- (a) Value of investment in Meru Ltd. as on 31st March, 2019 as per equity method in the consolidated financial statements of Sumeru Ltd.

	₹
Cost of Investment	3,00,000
Less: Share in Post-Acquisition Loss (1,00,00,000 X 35%)	(35,00,000)
Less: Unrealised gain on inventory left unsold with Meru Limited $[(50,000 / 3,50,000) \times 1,00,000] \times 35\%$	(5,000)
Carrying value as per Equity method	2,64,95,000

- (b) Value of investment in Meru Limited as on 31st March, 2019 as per equity method in the consolidated financial statements of Sumeru Limited.

	₹
Cost of Investment	3,00,00,000
Add: Share in Post-Acquisition Profit (1,50,00,000x 35%)	52,50,000
Less: Unrealised gain on inventory left unsold with Meru Ltd. $[(50,000 / 3,50,000) \times 1,00,000] \times 35\%$	(5,000)
Less: Dividend (75,00,000 x 35%)	<u>(26,25,000)</u>
Carrying value as per Equity method	<u>3,26,20,000</u>

Q19: An entity P (parent) has two wholly-owned subsidiaries - X and Y, each of which has an ownership interest in an 'associate', entity Z. Subsidiary X is a venture capital organisation. Neither of the investments held in associate Z by subsidiaries X and Y is held for trading. Subsidiary X and Y account for their investment in associate Z at fair value through profit or loss in accordance with Ind AS 109 and using the equity method in accordance with Ind AS 28 respectively.

How should P account for the investment in associate Z in the following scenarios:

Scenario 1: Where both investments in the associate result in significant influence on a stand-alone basis - Subsidiary X and Y ownership interest in associate Z is 25% and 20% respectively.

Scenario 2: When neither of the investments in the associate results in significant influence on a stand-alone basis, but do provide the parent with significant influence on a combined basis - Subsidiary X and Y ownership interest in associate Z is 10% each.

Scenario 3: When one of the investments in the associate results in significant influence on a stand-alone basis and the other investment in the associate does not result in significant influence on a stand-alone basis - Subsidiary X and Y ownership interest in associate Z is 30% and 10% respectively.

Assume there is significant influence if the entity has 20% or more voting rights.

[RTP May 2020]

Ans: Paragraph 18 of Ind AS 28 states that, "when an investment in an associate or a joint venture is held by, or is held indirectly through, an entity that is a venture capital organisation, or a mutual

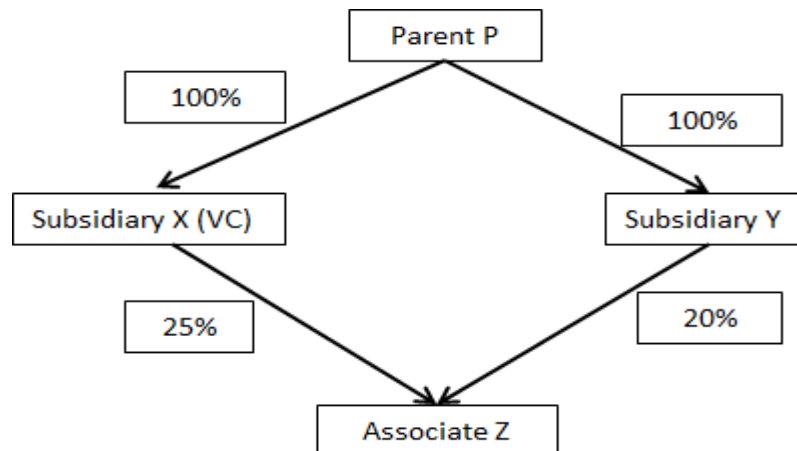
fund, unit trust and similar entities including investment-linked insurance funds, the entity may elect to measure investments in those associates and joint ventures at fair value through profit or loss in accordance with Ind AS 109. An entity shall make this election separately for each associate or joint venture, at initial recognition of the associate or joint venture.”

Paragraph 19 of Ind AS 28 provides that, “when an entity has an investment in an associate, a portion of which is held indirectly through a venture capital organisation, or a mutual fund, unit trust and similar entities including investment-linked insurance funds, the entity may elect to measure that portion of the investment in the associate at fair value through profit or loss in accordance with Ind AS 109 regardless of whether the venture capital organisation has significant influence over that portion of the investment.

If the entity makes that election, the entity shall apply the equity method to any remaining portion of its investment in an associate that is not held through a venture capital organisation”.

Therefore, fair value exemption can be applied partially in such cases.

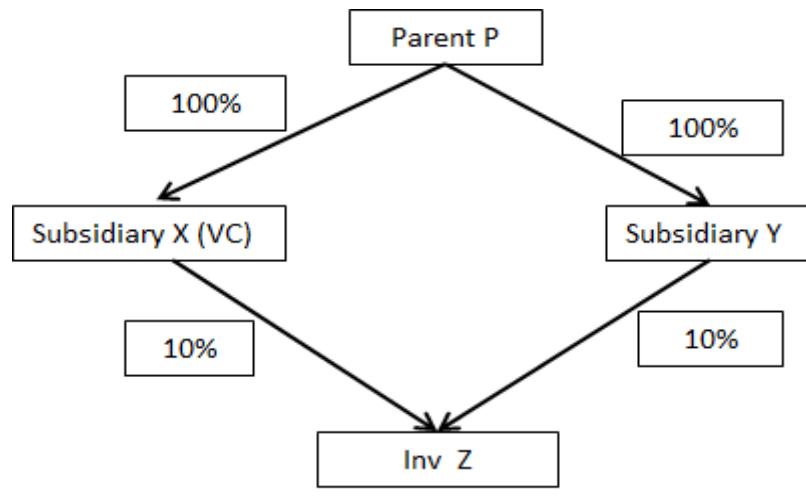
Scenario 1: Where both investments in the associate result in significant influence on a stand-alone basis.



In the present case, in accordance with paragraph 19 of Ind AS 28, P must follow equity method of accounting for its 20% interest held by Y.

Under the partial use of fair value exemption, P may elect to measure the 25% interest held by X at fair value through profit or loss.

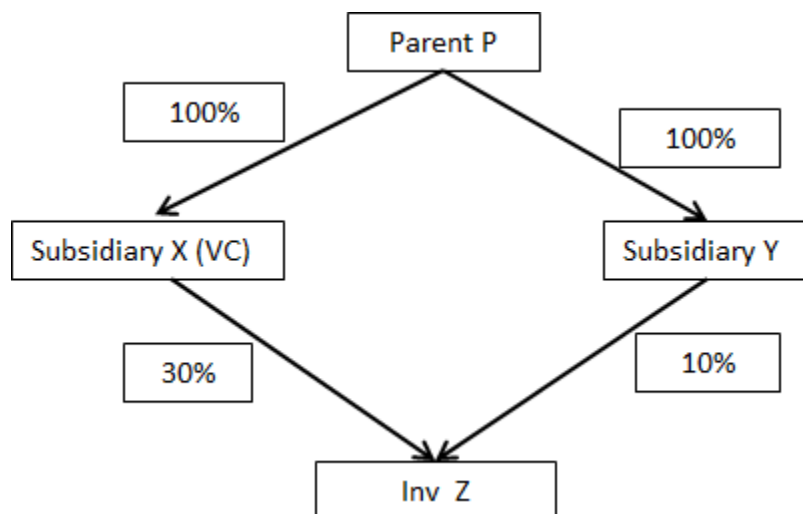
Scenario 2: When neither of the investments in the associate results in significant influence on a stand-alone basis, but do provide the parent with significant influence on a combined basis.



In the present case in accordance with the paragraph 19 of Ind AS 28, P must follow equity method of accounting for its 10% interest held by Y, even though Y would not have significant influence on a stand-alone basis.

Under the partial use of fair value exemption, P may elect to measure the 10% interest held by X at fair value through profit or loss.

Scenario 3: When one of the investments in the associate results in significant influence on a stand-alone basis and the other investment in the associate does not result in significant influence on a stand-alone basis



In the present case, in accordance with paragraph 19 of Ind AS 28, P must follow equity method of accounting for its 10% interest held by Y, even though Y would not have significant influence on a stand-alone basis.

Under the partial use of fair value exemption, the P may elect to measure the 30% interest held by X at fair value through profit or loss.

Q20: X Ltd. acquired a 10% interest in V Ltd. for ₹ 50,000 on 1st June, 20X6. The investment in V Ltd. was accounted for as equity investment (not held for trading) for which irrevocable option has been availed for subsequent measurement of financial assets at FVTOCI. X Ltd. recognized an increase in fair value of ₹ 30,000 in other comprehensive income for the year ended 31st March,

20X7.

X Ltd. acquired an additional 25% interest in V Ltd. for ₹ 2,00,000 on 1st April, 20X7 and achieved significant influence. The fair value of V Ltd.'s net assets was ₹ 2,50,000 at June, 20X6 and had increased to ₹ 4,00,000 on 1st April, 20X7. V Ltd. recorded profits after dividends of ₹ 1,00,000 between 1st June, 20X6 and 1st April, 20X7.

How should X Ltd. account for an investment in V Ltd. on account of piecemeal acquisition when such investment provides X Ltd. significant influence over V Ltd.? Pass necessary journal entries for the same. [RTP May 2025]

Ans: While applying equity method, paragraph 10 of Ind AS 28 requires, the investment in an associate to be initially recognized at cost. However, it doesn't include any specific guidance on how to account for existing investment, which is accounted for under Ind AS 109, that subsequently becomes an associate or a joint venture. One may apply the fair value approach, by drawing an analogy from paragraph 42 of Ind AS 103.

Paragraph 42 of Ind AS 103, 'Business Combinations', deals with the situation where control over an acquiree is achieved in stages. In such a case, the acquirer shall remeasure its previously held equity interest in the acquiree at its acquisitions- date fair value and recognize the resulting gain or loss, if any, in profit or loss or OCI, as appropriate. In prior reporting periods, the acquirer may have recognized changes in the value of its equity interest in the acquiree on OCI. If so, the amount that was recognized in OCI shall be recognized on the same basis as would be required if the acquirer had disposed directly of the previously held equity interest.

On application of the above guidance, following accounting will be done:

Computation of goodwill on gaining significant influence on V Ltd.

Particulars	
Fair value of previously held 10% interest [2,00,000/25% x10%]	80,000
Fair value of additional 25% (amount paid)	<u>2,00,000</u>
Cost of investment in associate V Ltd.	2,80,000
Less: Fair value of identifiable net assets acquired (4,00,000 x 35%)	<u>(1,40,000)</u>
Goodwill	<u>1,40,000</u>

Journal Entries

Particulars		Amount (₹)	Amount (₹)
Investment A/c (10%)	Dr.	30,000	
To OCI (Equity)			30,000
Investment A/c (35%)	Dr.	2,80,000	
To Bank A/c			2,00,000
To Investment (FVTOCI) (10%)			80,000
OCI (Equity)	Dr.	30,000	
To Retained Earning			30,000

Q21: Beta Limited (investee) has issued 2,000 equity shares which are outstanding at the reporting date. On this date, Beta issues 1,000 share options to its employees, which can be converted into 1,000 equity shares of Beta. The grant-date fair value of each option issued is ₹ 1. The options will vest over five years and all 1,000 options are expected to vest. Beta recognises share-based remuneration expense of ₹ 200 in its profit or loss and an offsetting credit to equity in the current year. Alpha Limited (investor) holds 600 shares of Beta. Alpha has significant influence over Beta. Alpha recognises its share of the remuneration expense in its profit or loss as part of income from the equity-accounted investees. It records the offsetting credit as a reduction of its investment in Beta. At the end of the vesting period, all options vest and are exercised. The exercise price is ₹ 3 per option. The face value per share is ₹ 1.

Required

- (i) Pass journal entries in the books of Beta Limited and Alpha Limited for recording share-based payment expenses for the first year.
- (ii) Pass Journal entries for exercising of option in the 5th year, in the books of Beta Limited.
- (iii) In the books of Alpha Limited, compute the loss on dilution of shares of Beta Limited and pass journal entries for the same. Beta has net assets totalling ₹ 11,000, immediately before the shares are issued.

[RTP SEP 2025]

Ans: (i) Journal Entries to be recorded over the five-year vesting period:

		₹	₹
In Beta's books			
Share based payments remuneration (profit or loss)	Dr.	200	
To Shareholders' equity (ESOP reserve)			200
(To recognise share based payment at associate level)			
In Alpha's books			
Share based payment remuneration (profit or loss)	Dr.	60	
Investment in associate			60
(To recognise share based payment at investor level)			

(ii) Journal Entries in the books of Beta to recognise share issue:

		₹	₹
Cash	Dr.	3,000	
Shareholders' equity (ESOP reserve)	Dr.	1,000	
To Share capital			1,000
To Share premium			3,000
(To recognise exercise of options at the associate level)			

(iii) Accounting in the Financial Statements of Alpha

The issue of new share options results in a dilution of Alpha's interest in Beta by 10% [30% - {(600/(2,000+1000)×100)]. However, Alpha maintains significant influence over Beta.

Alpha calculates loss on dilution as below.

Alpha's share of net assets before exercise (11,000 x 30%)	3,300
Alpha's share of net assets after exercise ((11,000+3,000) x 20%)	<u>(2,800)</u>
Cumulative adjustment required	500
Less: Adjustment previously recognized for share based payment expense (60 x 5 years)	<u>(300)</u>
Loss on dilution	<u>200</u>

Alpha passes the following entry to recognise dilution

		₹	₹
Loss on dilution (profit or loss) Dr.		200	
To Investment in associate			200
(To recognize dilution of investment in associate)			