1. The Conceptual Framework for Financial Reporting under IND AS (hereinafter the 'Conceptual Framework under Ind AS'): The Framework presents the
   - main ideas, concepts and principles

   upon which all IND AS, and therefore financial statements, are based.
   It is a set of
   - theoretical principles and
   - concepts

   that trigger the preparation and presentation of financial statements.

   Important Note: It is not a Standard and it does not override any standard or any requirement in any standard.

2. Importance of a conceptual framework
   (i) If no conceptual framework existed, then accounting standards would be produced on a messy basis as particular issues and circumstances arose and might be inconsistent with one another, or perhaps even contradictory.
   (ii) It also acts as a reference point
   - for the preparers of financial statements if no accounting standard governs a particular transaction.

3. The purpose of the Conceptual Framework is to assist:
   (i) Standard-setter for formulating IND AS (Assist ICAI in formulation of Ind AS)
   (ii) Preparers of financial statements in applying IND AS
   - to develop consistent accounting policies when no Ind AS applies to a particular transaction or event, OR
   - When an Ind AS allows a choice of accounting policy

   (iii) Users of financial statements in interpreting and understanding the information contained in financial statements.
   (iv) Auditors in forming an opinion as to whether financial statements conform to IND AS.

4. Meaning of Financial Reporting:
   - It refers to the all financial communication of financial information/result to end users.
   - It covered how an entity performed over the time.

5. Objectives of the Financial Reporting:
   - to track, analyse and report your business performance
   - to provide financial information about the reporting entity that is useful to current investors and potential investors, lenders and other users in making decisions relating to providing resources to the entity.

   If end users are going to make any decision then they require information that will help them to assess:
   (i) an entity's potential future cash flows, and
   (ii) management's stewardship of the entity's economic resources.

   To assess and examine an entity's future cash flows, business performance and the financial health of the business users need information about:
   (i) economic resources of the entity e.g. assets
   (ii) economic claims against the entity e.g. liabilities and equity
   (iii) changes in economic resources and claims e.g. income and expenses.

6. The qualitative characteristics of useful financial information: are the attributes that make the information provided in financial statements useful to users.
The Framework splits qualitative characteristics into 2 categories:

A. Fundamental qualitative characteristics

(i) Relevance: That information is relevant, which is likely to influence the economic decisions by the users is said to be relevant.

- Such information may help the users to evaluate past, present or future events.
- Relevance requires consideration of materiality. An item is material if omitting, misstating or obscuring it would influence the economic decisions of users.

(ii) Faithful representation: The transactions & other events that it mean to represent, they must be accounted for and presented in accordance with their substance and economic reality and not merely their legal form. This is known as 'substance over form'.
The financial information provided is considered faithfully, if these have following characteristics:

(a) Substance over form: reported in terms of their substance and economic reality not merely on the basis of their legal form;
(b) Neutral i.e. free from bias.
(c) Prudence is exercised in reporting: Prudence means that assets and income are not overstated and liabilities and expenses are not understated. But this does not mean that assets and income should be purposefully understated, or liabilities and expenses purposefully overstated.
(d) Completeness.

B. Enhancing qualitative characteristics:

(i) Comparability: The financial statements should permit both inter-firm and intra-firm comparison.

(ii) Understandability: FS should present information in a manner as to be readily understandable by the users with reasonable knowledge of business and economic activities.

(iii) Verifiability: Verification can be done

- Direct i.e. counting Stock or cash.
- Indirect i.e. checking the inputs to a model and recalculation the outputs using the same methodology.
- Confirmation of any balance by a third party.

(iv) Timeliness: having information available to decision makers in time to be capable of influencing their decisions.

Important points:

(i) Enhancing qualitative characteristics cannot make information useful if the information is irrelevant or if it is not a faithful representation.

(ii) Cost constraint:
(a) When developing IND AS standards, the ICAI assesses whether the benefits of reporting particular information compensate the costs involved in providing it.
(b) The benefits of reporting information should justify the costs incurred in reporting it.

7. The Elements of Financial Statements: Items of financial statements can be classified in five broad groups depending on their economic characteristics:

Asset: (Economic resources)	A present economic resource controlled by the entity as a result of past event.
Liability: (Economic Claim)	A present obligation of the entity to transfer an economic resource as a result of past events.
Equity: (Economic Claim)	The residual interest in the assets of an enterprise after deducting all its liabilities (i.e. net assets of an entity).
Income/gain: (Changes in economic resources & claims)	Increase in economic benefits during the accounting period in the form of inflows or enhancement of assets or decreases in liabilities that result in increase in equity other than those relating to contributions from equity participants
Expense/loss: (Changes in economic resources & claims)	Decrease in economic benefits during the accounting period in the form of outflows or decrease of assets or increase of liabilities that result in decrease in equity other than those relating to distributions to equity participants.

Other changes in economic resources and claims
(i) Contributions from holders of equity claims, and distributions to them.
(ii) Exchanges of assets or liabilities that do not result in increases or decreases in equity.

8. Evaluate the decisions made by management on recognition, derecognition & measurement.
A. Recognition: is the process of capturing an item
- that meets the definition of one of the elements of financial statements. (an asset, a liability, equity, income or expenses)
- for inclusion in the statement of financial position or the statement of profit & loss.

The amount at which an asset, a liability or equity is recognised in the statement of financial position is referred to as its 'carrying amount'.

However, not all items that meet the definition of one of those elements are recognised.

Elements are recognised if recognition provides: users with useful financial information. Recognition must provide:
- Relevant information
- a faithful representation of the asset or liability, and resulting income, expenses or equity movements.

However
(a) If there is uncertainty over the existence of the element or if there is a low probability of an inflow or outflow of economic resources
    - Then recognition might not provide relevant information

E.g. As per IND AS 37 prohibits recognition of contingent liabilities & assets because it is not probable that resources will flow from or to the reporting entity.

(b) If there is a very high degree of measurement uncertainty.

- Recognition of an element might not provide a faithful representation

E.g. As per IND AS 38 internally generated brands, mastheads, publishing titles, customer lists and items similar in substance should not be recognised as intangible assets because Expenditure on such items cannot be distinguished from the cost of developing the business as a whole.

Recognition of an element is appropriate or not, it is required Judgement to decide, this is why specific recognition criteria vary from one IND AS Standard to another.

If an asset or liability is not recognised, disclosures may be required.

B. Derecognition: is the removal of all or part of a recognised asset or liability from SOFP. Derecognition normally occurs when that item no longer meets the definition of

- an asset: losses control of the asset, or
- a liability: has no present obligation for the liability.

Accounting for derecognition should faithfully represent the changes in an entity's net assets. This is achieved by:

- derecognising any transferred, expired or consumed component and recognising a gain or loss on such derecognising, and
- recognising any retained component.

However, derecognition would not be appropriate

- if an entity has apparently transferred an asset
- but retains exposure to significant variations (positive or negative) in the amount of economic benefits that may be produced by the asset

E.g. X Ltd. sells a Land and Building for ₹ 5 million (had a fair value of ₹ 18 million on the date of sale) and retains the right to buy it back for ₹ 6.9 million in three years' time. Land and building price is expected to rise. In this case entity does not derecognise the land and building from its statement of financial position because the entity has not lost control over the land and building. It has ability to buy the land and building back for substantially less than fair value enables it to benefit from future price rises. The cash received would be recognised as a loan liability.

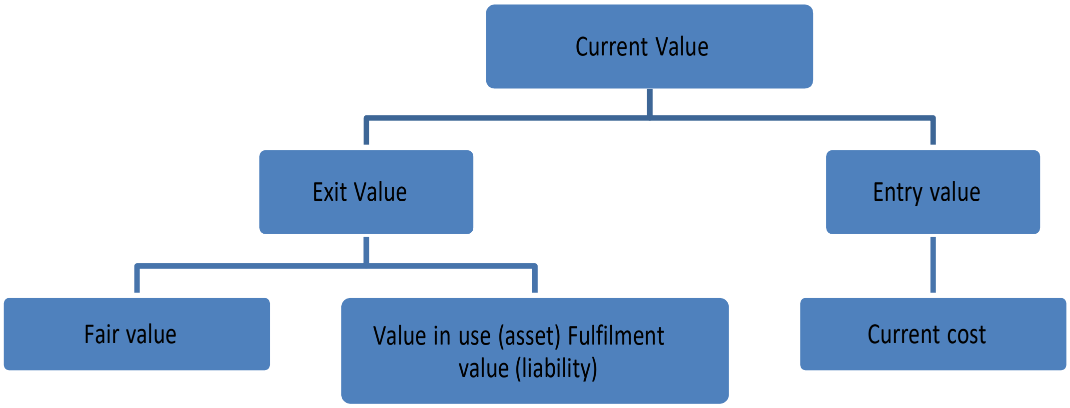
C. Measurement: Elements must be quantified in monetary terms for recognised in the financial statements.
The Conceptual Framework outlines two broad measurement bases:

(a) Historical cost:

Assets = Consideration paid (+) transaction costs
Liabilities = Considerationreceived (-) transaction costs

Note: When an asset is acquired or created (say, a loan is given by a parent to a subsidiary), or a liability is incurred or taken on, as a result of an event that is not a transaction on market terms (say, at a discounted interest rate), it may not be possible to identify a cost, or the cost may not provide relevant information about the asset or liability. In some such cases, a current value of the asset (say, fair value) or liability is used as a deemed cost on initial recognition and that deemed cost is then used as a starting point for subsequent measurement at historical cost (say, amortised cost in case of the loan).

(b) Current value (this includes fair value, value-in-use, and current cost).



Fair value: Price that would be received to sell an asset, or paid to transfer a liability, in an orderly transaction between market participants at the measurement date.

- It Reflects the perspective of market participants—participants in a market to which the entity has access.

Value in use / Fulfilment value:
Value in use: PV of the cash flows, or other economic benefits, that an entity expects to derive from the use of an asset and from its ultimate disposal.

Fulfilment value: PV of the cash, or other economic resources, that an entity expects to be obliged to transfer as it fulfils a liability.

- These reflect entity-specific assumptions rather than assumptions by market participants

Current cost: Value determined on each measurement date instead of date of acquisition of asset or incurrence of liability n case of historical cost. Here
Assets: Consideration that would be paid(+)transaction costs that would be incurred
Liabilities: Consideration that would be received(-)transaction costs that would be incurred

Selection of a measurement base: The information provided by the measurement base must be useful (means it must be relevant and offer a faithful representation of the transactions that have occurred)

When selecting a measurement basis, the Conceptual Framework states that relevance is maximised if the following two are considered:
(a) The characteristics of the asset and/or liability
(b) The ways in which the asset and/or liability contribute to future cash flows.

Measurement of equity: The total carrying amount of equity (total equity) is not measured directly. It equals the total of the carrying amounts of all recognised assets less the total of the carrying amounts of all recognised liabilities.

9. Presentation and disclosure:

A. Effective presentation and disclosure:

- It allowing entities to flexibly report relevant information about their financial performance & position, and requiring information that enables comparisons to be drawn for more than one year and with other entities.
- The ICAI believes that:
  - ✓ Entity specific information is more useful than standardised descriptions.
  - ✓ Duplication makes financial information less understandable.

B. Offsetting: classifies dissimilar items together & therefore is generally not appropriate.

C. Classification: of an asset or liability into separate components may provide relevant information if the components have different characteristics. E.g. X Ltd. had borrowing of ₹ 300,000 out of which ₹ 50,000 is due for repayment within 12 months. In this case ₹ 50,000 shall be presented as a current liability and the remaining ₹ 250,000 is presented as a non-current liability.

D. Aggregation: is adding together of assets, liabilities, equity, income or expenses that have shared characteristics and are included in the same classification.

- Aggregation makes information more useful by summarising a large volume of detail. However, aggregation conceals some of that detail. Hence, a balance needs to be found so that relevant information is not obscured either by a large amount of insignificant detail or by excessive aggregation.
- Different levels of aggregation may be needed in different parts of the financial statements. E.g. typically, B/S and the statement of profit and loss provide summarised information and more detailed information is provided in the notes.

E. Profit or loss and other comprehensive income

Income and expenses are classified and included either:

(a) in the profit or loss section of statement of profit and loss; or

(b) outside the profit or loss section of statement of profit and loss, in OCI.

Because the profit or loss section of statement of profit and loss is the primary source of information about an entity's financial performance for the period, all income and expenses are, in principle, included in that statement.

However, in formulating IND AS, the ICAI may decide in exceptional circumstances that income or expenses arising from a change in the current value of an asset or liability are to be included in OCI when doing so would result in the profit or loss section of statement of profit and loss providing more relevant information, or providing a more faithful representation of the entity's financial performance for that period.

In principle, income and expenses included in OCI in one period are reclassified from OCI into the profit or loss in a future period when doing so results in the profit or loss providing more relevant information, or providing a more faithful representation of the entity's financial performance for that future period. However, if, for example, there is no clear basis for identifying the period in which reclassification would have that result, or the amount that should be reclassified, the ICAI may, in formulating IND AS, decide that income and expenses included in OCI are not to be subsequently reclassified.

10. Objective and scope of financial statements: The objective of financial statements is to provide financial information about the reporting entity's:
    - assets, liabilities and equity; and
    - income and expenses
      (i.e. the elements of the financial statements) that is useful to users of financial statements in assessing:
    - the prospects for future net cash inflows to the reporting entity, and
    - management's stewardship of the entity's economic resources. Such financial information is provided:
      (a) in the balance sheet, by recognising assets, liabilities and equity;
      (b) in the statement of profit and loss, by recognising income and expenses; and
      (c) in other statements and notes, by presenting & disclosing information about:
        (i) recognised assets, liabilities, equity, income and expenses, including information about their nature and about the risks arising from those recognised assets and liabilities;
        (ii) assets and liabilities that have not been recognised, including information about their nature and about the risks arising from them;
        (iii) cash flows;
        (iv) contributions from holders of equity claims & distributions to them; and
        (v) the methods, assumptions and judgements used in estimating the amounts presented or disclosed, and changes in those methods, assumptions and judgements.

11. A reporting entity is an entity that is required, or chooses, to prepare financial statements. A reporting entity can be a single entity or a portion of an entity or can comprise more than one entity. A reporting entity is not necessarily a legal entity.
    Sometimes one entity (parent) has control over another entity (subsidiary). If a reporting entity comprises both the parent and its subsidiaries, the reporting entity's financial statements are referred to as 'consolidated financial statements'.
    Consolidated financial statements show the parent and its subsidiaries as a single economic entity. This information is important for investors in the parent because their economic returns are dependent on distributions from the subsidiary to the parent.
    However, unconsolidated financial statements also provide useful information to investors in a parent company but they are not a substitute for information provided in consolidated financial statements.

12. Financial capital maintenance vs. Physical capital maintenance
    A. Financial Capital maintenance (Considered inflation) Under this concept, a profit is earned only if the financial amount of the net assets at the end of the period exceeds the financial amount of net assets at the beginning of the period, after excluding any distribution to, and contribution from, owners during the period.

B. Physical / Operating Capital maintenance (PCM)/(OCM): (Linked with current cost / replacement cost) Under this concept, a profit is earned only if the physical productive or operating capability of the entity at the end of the period exceeds the physical productive capacity at the beginning of the period, after excluding any distributions to, and contributions from, owners during the period.

Examples:

1. A trader commenced business on 01/01/20X1 with INR 12,000 represented by 6,000 units of a certain product at INR 2 per unit. During the year 20X2 he sold these units at INR 3 per unit and had withdrawn INR 6,000. Thus:
   Opening Equity = INR 12,000 represented by 6,000 units at INR 2 per unit.
   Closing Equity = INR 12,000 (INR 18,000 – INR 6,000) represented entirely by cash.
   Retained Profit = INR 12,000 – INR 12,000 = Nil.
   The trader can start year 20X3 by purchasing 6,000 units at INR 2 per unit once again for selling them at INR 3 per unit. The whole process can repeat endlessly if there is no change in purchase price of the product.

2. In the previous example A, suppose that the average price indices at the beginning and at the end of year are 100 and 120 respectively.
   Opening Equity = INR 12,000 represented by 6,000 units at INR 2 per unit.
   Opening equity at closing price = (INR 12,000 / 100) x 120 = INR 14,400 (6,000 x INR 2.40)
   Closing Equity at closing price = INR 12,000 (INR 18,000 – INR 6,000) represented entirely by cash.
   Retained Profit = INR 12,000 – INR 14,400 = (-) INR 2,400
   The negative retained profit indicates that the trader has failed to maintain his capital. The available fund INR 12,000 is not sufficient to buy 6,000 units again at increased price INR 2.40 per unit. In fact, he should have restricted his drawings to INR 3,600 (INR 6,000 – INR 2,400). Had the trader withdrawn INR 3,600 instead of INR 6,000, he would have left with INR 14,400, the fund required to buy 6,000 units at INR 2.40 per unit

13. Limitations of General purpose financial reports:

(i) Do not and cannot provide all of the information that existing and potential investors, lenders and other creditors need. Those users need to consider pertinent information from other sources, for example, general economic conditions and expectations, political events and political climate, and industry and company outlooks;

(ii) are not designed to show the value of a reporting entity; but they provide information to help existing and potential investors, lenders and other creditors to estimate the value of the reporting entity; and

(iii) are not primarily directed to other parties, such as regulators and members of the public other than investors, lenders and other creditors.

PRACTICAL QUESTIONS

1. As at 31 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 31 March 20X2, and also evaluate this transaction in the context of the Conceptual Framework.

   Solution:

   Accounting Treatment:

   Trade Receivables fall within the ambit of financial assets under Ind AS 109, Financial Instruments. Thus, the issue in question is whether the factoring arrangement entered into with Samantha Ltd. requires Natasha Ltd. to derecognize the trade receivables from its financial statements.

   As per Para 3.2.3, 3.2.4, 3.2.5 and 3.2.6 of Ind AS 109, Financial Instruments, an entity shall derecognise a financial asset when, and only when:

   (a) the contractual rights to the cash flows from the financial asset expire, or

   (b) it transfers the financial asset or substantially all the risks and rewards of ownership of the financial asset to another party.

   In the given case, since the trade receivables are appearing in the Balance Sheet of Natasha Ltd. as at 31 March 20X2 and are expected to be collected, the contractual rights to the cash flows have not expired.

   As far as the transfer of the risks and rewards of ownership is concerned, the factoring arrangement needs to be viewed in its substance, rather than its legal form. Natasha Ltd. has transferred the receivables to Samantha Ltd. for cash of ₹ 250 crores, and yet, it remains liable for making good any shortfall between ₹ 250 crores and the amount collected by Samantha Ltd. Thus, in substance, Natasha Ltd. is effectively liable for the entire ₹ 250 crores, although the shortfall would not be such an amount. Accordingly, Natasha Ltd. retains the credit risk despite the factoring arrangement entered.

   It is also explicitly stated in the agreement that Samantha Ltd. would be liable to pay to Natasha Ltd. any amount collected more than ₹ 250 crores, after retaining an amount towards interest. Thus, Natasha Ltd. retains the potential rewards of full settlement.

   A perusal of the above clearly shows that substantially all the risks and rewards continue to remain with Natasha Ltd., and hence, the trade receivables should continue to appear in the Balance Sheet of Natasha Ltd. The immediate payment (i.e. consideration as per the factoring agreement) of ₹ 250 crores by Samantha Ltd. to Natasha Ltd. should be regarded as a financial liability, and be shown as such by Natasha Ltd. in its Balance Sheet.

2. Explain the criteria in the Conceptual Framework for Financial Reporting for the recognition of an asset and discuss whether there are inconsistencies with the criteria in Ind AS 38, Intangible Assets.

   Solution: The Conceptual Framework defines an asset as a present economic resource controlled by the entity as a result of past events. An economic resource is a right that has the potential to produce economic benefits. Assets should be recognized if they meet the Conceptual Framework definition of an asset and such recognition provides users of financial statements with information that is useful (i.e. it is relevant as well as results in faithful representation). However, the criteria of a cost-benefit analysis always exists i.e. the benefits of the information must be sufficient to justify the costs of providing such information. The recognition criteria outlined in the Conceptual Framework allows for flexibility in the application in amending or developing the standards.

   Para 8 of Ind AS 38, Intangible Assets defines an intangible asset as an identifiable non-monetary asset without physical substance. Further, Ind AS 38 defines an asset as a resource:

   (a) controlled by an entity as a result of past events; and

   (b) from which future economic benefits are expected to flow to the entity.

Furthermore, Para 21 of Ind AS 38 states that an intangible asset shall be recognised if, and only if:
(a) it is probable that the expected future economic benefits that are attributable to the asset will flow to the entity; and
(b) the cost of the asset can be measured reliably.

This requirement is applicable both in case of an externally acquired intangible asset or an internally generated intangible asset. The probability of expected future economic benefits must be based on reasonable and supportable assumptions that represent management's best estimate of the set of economic conditions that will exist over the useful life of the asset. Further, as per Para 33 of Ind AS 38, the probability recognition criterion is always considered to be satisfied for intangible assets acquired in business combinations. If the recognition criteria are not satisfied, Ind AS 38 requires the expenditure to be expensed as and when it is incurred.
It is notable that the Conceptual Framework does not prescribe a 'probability criterion'. As long as there is a potential to produce economic benefits, even with a low probability, an item can be recognized as an asset according to the Conceptual Framework. However, in terms of intangible assets, it could be argued that recognizing an intangible asset having low probability of generating economic benefits would not be useful to the users of financial statements given that the asset has no physical substance.

The recognition criteria and definition of an asset under Ind AS 38 are different as compared to those outlined in the Conceptual Framework. To put in simple words, the criteria in Ind AS 38 are more specific, but definitely do provide information that is relevant and a faithful representation. When viewed from the prism of relevance and faithful representation, the requirements of Ind AS 38 in terms of recognition appear to be consistent with the Conceptual Framework.

3. The directors of Hind Ltd. are particular about the usefulness of the financial statements. They have opined that although Ind AS implement a fair value model, Ind AS are failing in reflecting the usefulness of the financial statements as they do not reflect the financial value of the entity.
Discuss the views of the directors as regards the use of fair value in Ind AS and the fact that the Ind AS do not reflect the financial value of an entity, making special reference to relevant Ind AS and the Conceptual Framework.

Solution:

Usage of Fair Value in Ind AS:

Treatment under Ind AS:

The statement of the directors regarding Ind AS implementing a fair value model is not entire accurate. Although Ind AS do use fair value (and present value), it is not a complete fair value system. Ind AS are often based on the business model of the entity and on the expectations of realizing the asset- and liability-related cash flows through operations and transfers.
It is notable that what is preferred is a mixed measurement system, with some items being measured at fair value while others measured at historical cost.

About Fair Value (Ind AS 113)

Ind AS 113 defines fair value as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. This price is an exit price.
Ind AS 113 has given consistency to the definition and application of fair value, and this consistency is applied across other Ind AS, which are generally required to measure fair value in accordance with Ind AS 113. However, it cannot be implied that Ind AS requires all assets and liabilities to be measured at fair value. Rather, many entities measure most items at depreciated historical costs, although the exception being in the case of business combinations, where assets and liabilities are recorded at fair value on the date of acquisition. In other cases, usage of fair value is restricted.

Examples of use of fair value in Ind AS:

(a) Ind AS 16 Property, Plant and Equipment permits revaluation through other comprehensive income, provided it is carried out regularly.
(b) Disclosure of fair value of Investment Property in Ind AS 40, while the companies account for the same under the cost model.
(c) Ind AS 38 Intangible Assets allows measurement of intangible assets at fair value with corresponding changes in equity, but only if the assets can be measured reliably by way of existence of an active market for them.

(d) Ind AS 109 Financial Instruments requires some financial assets and liabilities to be measured at amortized cost and others at fair value. The measurement basis is largely determined by the business model for that financial instrument. Where the financial instruments are carried at fair value, depending on the category and circumstances, the movement in the fair value (gain or loss) is either recognized in profit or loss or in other comprehensive income.

Financial value of an entity

Although Ind AS makes use of fair values in the measurement of assets and liabilities, the financial statements prepared under Ind AS are not intended to reflect the aggregate value of the entity, as could be the notion among people. As discussed, the Conceptual Framework specifically states that general purpose financial statements are not intended to show the value of a reporting entity. Furthermore, such an attempt would not be fruitful as certain internally generated intangible assets cannot be recognized under Ind AS. Instead, the objective of general purpose financial reports is to provide financial information about the reporting entity which would be useful to existing and potential investors, lenders and other creditors in making decisions about providing resources to the entity.

It is only in the case of acquisition of an entity by another entity and subsequent consolidation in group accounts that an entity's net assets are reported at fair value.

4. Everest Ltd. is a listed company having investments in various subsidiaries. In its annual financial statements for the year ending 31 March 20X2 as well as 31 March 20X3, Everest Ltd. classified Kanchenjunga Ltd. a subsidiary as 'held-for-sale' and presented it as a discontinued operation. On 1 November 20X1, the shareholders had authorized the management to sell all of its holding in Kanchenjunga Ltd. within the year. In the year to 31 March 20X2, the management made a public announcement of its intention to sell the investment but did not actively try to sell the subsidiary as it was still operational within the Everest group.

Certain organizational changes were made by Everest Ltd. during the year to 31 March 20X3, thereby resulting in additional activities being transferred to Kanchenjunga Ltd. Additionally, during the year ending 31 March 20X3, there had been draft agreements and some correspondence with investment bankers, which showed in principle only that Kanchenjunga was still for sale.

Discuss whether the classification of Kanchenjunga Ltd. as held for sale and its presentation as a discontinued operation is appropriate, by referring to the principles of the relevant Ind AS and evaluating the treatment in the context of the Conceptual Framework for Financial Reporting.

Solution: Kanchenjunga Ltd. is a disposal group in accordance with Ind AS 105, Non-current Assets Held for Sale and Discontinued Operations. Disposal group can be defined as a group of assets to be disposed of, by sale or otherwise, together as a group in a single transaction, and liabilities directly associated with those assets that will be transferred in the transaction.

Para 6 of Ind AS 105 provides that a disposal group shall be classified as held for sale if its carrying amount will be recovered principally through a sale transaction rather than through continuing use. Ind AS 105 is particularly strict as far as the application of held for sale criteria is concerned, and often the decision to sell an asset or a disposal group is made well before the criteria are met.

Thus, as per Ind AS 105, for the asset (or disposal group) to be classified as held for sale, it must be available for immediate sale in its present condition subject only to terms that are usual and customary for sales of such assets (or disposal groups) and its sale must be highly probable.

For the sale to be highly probable:

- The appropriate level of management must be committed to a plan to sell the asset (or disposal group).
- An active programme to locate a buyer and complete the plan must have been initiated.
- The asset (or disposal group) must be actively marketed for sale at a price that is reasonable in relation to its current fair value.
- The sale should be expected to qualify for recognition as a completed sale within one year from the date of classification.
- It is unlikely that significant changes to the plan will be made or that the plan will be withdrawn.

In the given case, the draft agreements and correspondence with investment bankers are not specific enough to fit in the points above to prove that the criteria for held for sale was met at that date. Additional information would be needed to confirm that the subsidiary was available for immediate sale, and that it was being actively marketed at an appropriate price so as to satisfy the criteria in the year to 31 March 20X2.

Further, the organizational changes made by Everest Ltd. in the year 20X2-20X3 are a good indicator that Kanchenjunga Ltd. was not available for immediate sale in its present condition at the point of classification. The fact that additional activities have been given to Kanchenjunga Ltd. indicate that the change wasn't insignificant. The shareholders had authorized for a year from 1 November 20X1. There is no evidence that this authorization extended beyond 1 November 20X2.

Conclusion:

Based on the information provided in the given case, it appears that Kanchenjunga Ltd. should not be classified by Everest Ltd. as a subsidiary held for sale. Instead, the results of the subsidiary should be reported as a continuing operation in the financial statements for the year ending 31 March 20X2 and 31 March 20X3.

Evaluation of treatment in context of the Conceptual Framework

The Conceptual Framework states that the users need information to allow them to assess the amount, timing and uncertainty of the prospects for future net cash inflows. Highlighting the results of discontinued operations separately equips users with the information that is relevant to this assessment as the discontinued operation will not contribute to cash flows in the future.

If a company has made a firm decision to sell the subsidiary, it could be argued that the subsidiary should be classified as discontinued operation, even if the criteria to classify it as 'held for sale' as per Ind AS 105 have not been met, because this information would be more useful to users. However, Ind AS 105 criteria was developed with high degree of strictness on classification. Accordingly, this decision could be argued to be in conflict with the Conceptual Framework.

5. The directors of Jayant Ltd. have received the following email from its majority shareholder:

To: Directors of Jayant Ltd. Re: Measurement

I recently read an article published in the financial press about the 'mixed measurement approach' that is used by lots of companies. I hope Jayant Ltd. does not follow such an approach because 'mixed' seems to imply 'inconsistent'. I believe that consistency is of paramount importance, and hence feel it would be better to measure everything in a uniform manner. It would be appreciated if you could provide further information at the next annual general meeting on measurement bases, covering what approach is taken by Jayant Ltd. and why, and the potential effect such an approach has on the investors trying to analyse the financial statements.

Prepare notes for the directors of Jayant Ltd. to discuss the issue raised in the shareholders' email with reference to the Conceptual Framework wherever appropriate.

Answer: 'Mixed measurement' approach implies that a company selects different measurement bases (e.g. historical cost or fair value) for its various assets and liabilities, rather than using one single measurement basis for all items. The measurement basis so selected should reflect the type of entity and the sector in which it operates and the business model that the entity adopts.

There are criticisms of the mixed measurement approach, particularly under the IND AS regime, because investors think that if different measurement bases are used for assets and liabilities, the resulting figures could lack relevance or exhibit little meaning.

It is however important to note that figures of items in the financial statements cannot be derived by following a one-size-fits-all approach. Such an approach may not provide relevant information to users. A particular measurement basis may be easier to understand, more verifiable and less costly to implement. Therefore, to state that 'mixed measurement' approach is 'inconsistent' is a poor argument. In reality, a mixed approach may actually provide more relevant information to the stakeholders.

The Conceptual Framework confirms the allowance of the usage of a mixed measurement approach in developing standards. The measurement methods included in the standards are those which the standard-setters believe provide the most relevant information and which most faithfully represent the underlying transaction or event. Based on the reactions to the convergence to Ind AS, it feels that most investors feel this approach is consistent with their analysis of financial statements. Thus, the arguments against a mixed measurement are far outweighed by the greater relevance achieved by such measurement bases.

Jayant Ltd. prepares its financial statements under Ind AS, and therefore applies the measurement bases permitted in Ind AS. Ind AS adopt a mixed measurement basis, which includes current value (fair value, value in use, fulfilment value and current cost) and historical cost.

Where an Ind AS allows a choice of measurement basis, the directors of Jayant Ltd. must exercise judgment as to which basis will provide the most useful information for its primary users. Furthermore, when selecting a measurement basis, measurement uncertainty should also be considered. The Conceptual Framework states that for some estimates, a high level of measurement uncertainty may outweigh other factors to such an extent that the resulting information may be of little relevance.

6. Mr. Unique commenced business on 1/04/17 with Rs 20,000 represented by 5,000 units of the product @ Rs 4 per unit. During the year 2017-18, he sold 5,000 units @ Rs 5 per unit. During 2017-18, he withdraws Rs. 4.000.
   - 31/03/18: Price of the product @ Rs. 4.60 per unit
   - Average price indices: 1/4/17: 100 & 31/3/18: 120

   Find out:
   (i) Financial capital maintenance at Historical Cost
   (ii) Financial capital maintenance at Current Purchasing Power
   (iii) Physical Capital Maintenance.

   Solution

   (a) Financial Capital Maintenance at historical costs

	Rs	Rs
Closing capital (Rs 25,000 – Rs 4,000)	-	21,000
Less: Capital to be maintained	20,000	(20,000)
		1,000

   (b) Financial Capital Maintenance at current purchasing power

	Rs	Rs
Closing capital (Rs 25,000 – Rs 4,000)		21,000
Less: Capital to be maintained		
Opening capital (At closing price) [5,000 x Rs 4.80 (120/100 X 4)]	24,000	
Introduction (At closing price)	Nil	(24,000)
Retained profit		(3,000)

   (c) Physical Capital Maintenance

	Rs	Rs
Closing capital (Rs 25,000 – Rs 4,000)		21,000
Less: Capital to be maintained		
Opening capital (At current cost) (5,000 x Rs 4.60)	23,000	
Introduction (At current cost)	Nil	(23,000)
Retained profit		(2,000)

7. Defense Innovators Limited is a public sector undertaking and is engaged in the construction of warships and submarines. XYZ Private Limited approached Defense Innovators Limited for construction of "specially designed" ships for it, which will be used by XYZ Private Limited for transportation of specific goods. The offer was accepted by the Defense Innovators Limited and both the companies entered into an agreement for the construction and delivery of 3 specially designed ships on 'Fixed Price' basis with variable component in respect to certain items.

   Base and depot (B & D) spares for all three ships shall be procured by Defense Innovators Limited and will be paid on the cost of the item with certain percentage.

   The contract states that "certain equipment" out of variable cost items, will be supplied by XYZ Private Limited at 'free of cost' for installation on board of ship. It is, therefore, to be noted as under:

   (i) Some equipment are procured by Defense Innovators Limited in the presence of the XYZ Private Limited's representative for technical scrutiny as well as negotiating the prices. The vendors of these equipment are paid by Defense Innovators Limited. The cost of the equipment along with the cost of installation and profit thereon is claimed and reimbursed by XYZ Private Limited to Defense Innovators Limited.

   (ii) There are certain other equipment for which orders are directly placed and also paid by the XYZ Private Limited. These equipment are known as 'Buyer Furnished Equipment (BFE)' and are delivered to the company 'free of cost' for installing in the ship. The labour cost of Installation of these are already included in the price component of the contract. BFEs are returned to the buyer after completion of the ship.

   The period required for construction of one ship was approximately four years.

Whether the cost of Buyer Furnished Equipment's (BFE's) supplied by XYZ Private Limited to Defense Innovators Limited for-installing the same in the ships can be considered as 'inventory' by Defense Innovators Limited and then on delivery of ship will be recognised as revenue in its books of account? Elaborate.

Solution: Before any item can be recognised as an inventory, it should meet the definition of 'asset' as given in the Conceptual Framework for Financial Reporting under Ind AS, issued by the Institute of Chartered Accountants of India as follows:

"An asset is a present economic resource controlled by the entity as a result of past events and economic resource is a right that has the potential to produce economic benefits".

The orders in respect of Buyer Furnished Equipment's (BFEs) are directly placed by the buyer and payment in respect of them is made by the buyer. These are then supplied to the company for installing in the ship and the buyer pays installation charges which are included in the contract price. Thus, the company has neither incurred any cost on BFEs nor any amount is recoverable on account of such equipment except installation charges. Accordingly, such equipment are not 'assets' that may be considered as a part of its contract work-in progress.

In fact, after installation in the ship, BFEs are returned to the buyer after completion of the ship. Thus, these are only held by the company in the capacity of a bailee. Since, it cannot be considered as an 'asset', therefore, it can neither be considered as 'inventory' nor as 'work-in-progress'.

Further, it can also not be considered as a part of sale value or revenue of the company as no consideration would be receivable with respect to the cost of such equipment.

On the basis of the above, it can be concluded that:

(i) The BFEs cannot be considered as inventories / Work-in-progress for Defense Innovators Limited.

(ii) The BFE's cost cannot be considered as part of sales value / contract revenue to Defense Innovators Limited.