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IFRS Notes

MCA issues amendments to Ind AS 102 and Ind AS 7

30 March 2017

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Background

The Ministry of Corporate Affairs (MCA), through its notification dated 16 February 2015, issued the Indian Accounting Standards (Ind AS), which are converged with International Financial Reporting Standards (IFRS) issued by the International Accounting Standards Board (IASB).

The IASB had issued amendments to IFRS 2, *Share-based Payment* on 20 June 2016 on completion of its project on classification and measurement of share-based payment transactions. The objective of these amendments is to clarify three issues relating to cash-settled share-based payment transactions.

In January 2016, IAS 7, *Statement of Cash Flows* had been amended as part of the IASB's broader disclosure initiative to improve presentation and disclosure in financial statements. For some time, investors have been calling for more disclosures on net debt, a term not defined in IFRS. The IASB has responded by requiring disclosures that enable users of financial statements to evaluate changes in liabilities arising from financing activities, including both changes arising from cash-flow and non-cash changes.

With Ind AS being applicable to large corporates from 1 April 2016, there is a need to keep Ind AS updated with revisions made to IFRS in order to maintain convergence. The amendments to Ind AS 102, *Share-based Payment* and Ind AS 7, *Statement of Cash Flows* notified by the MCA on 17 March 2017 are therefore in accordance with recent amendments to IFRS as issued by the IASB.

New development

Consequent to the amendments issued by the IASB, similar amendments were required in the Indian context to maintain convergence with IFRS. Accordingly, the MCA, on 17 March 2017 notified the Companies (Indian Accounting Standards) (Amendment) Rules, 2017, amending Ind AS 102 and Ind AS 7.

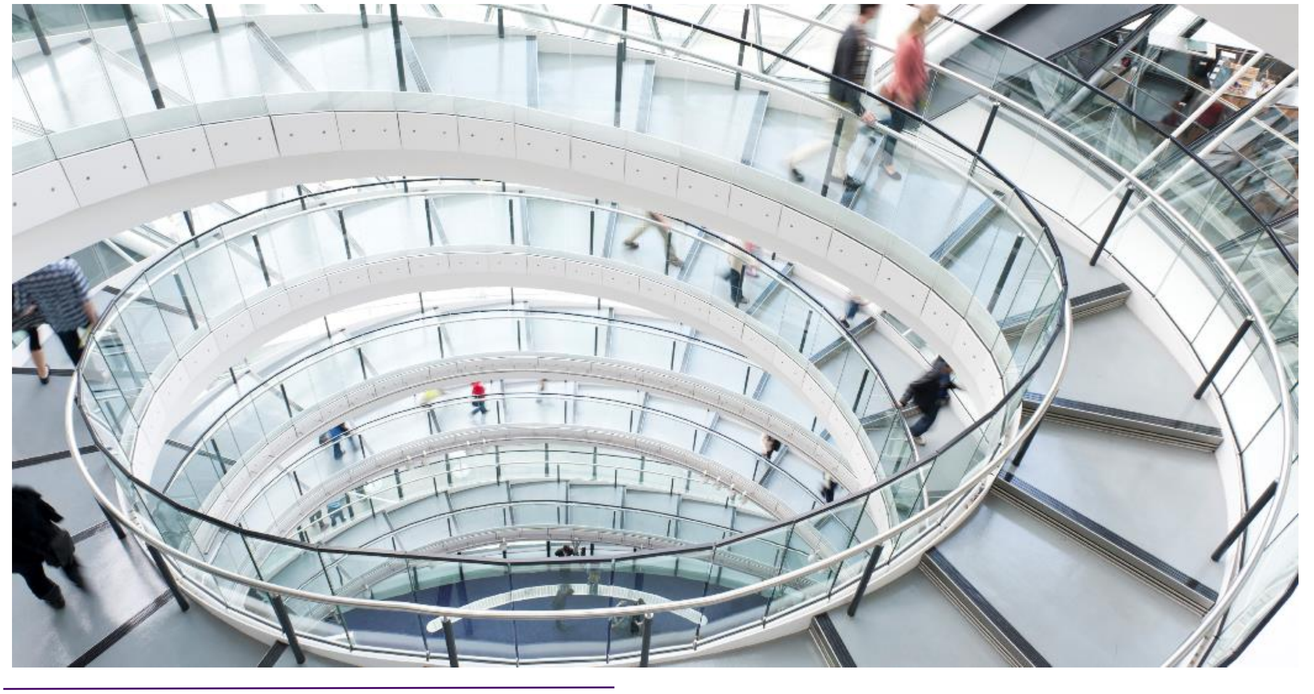
The amendments made to Ind AS 102 cover three accounting areas:

- Measurement of cash-settled share-based payments
- Classification of share-based payments settled net of tax withholdings and
- Accounting for a modification of a share-based payment from cash-settled to equity-settled.

These amendments could affect the classification and/or measurement of the share-based payment arrangements and potentially the timing and amount of expense recognised for new and outstanding awards.[1]

The amendments made to Ind AS 7 require certain additional disclosures to be made for changes in liabilities arising from financing activities on account of non-cash transactions to improve information provided to users of financial statements about an entity's financing activities.

This issue of IFRS notes provides an overview of these amendments.



[1] *Source: Clarifying share-based payment accounting, KPMG IFRG Limited's publication, June 2016*

Amendments to Ind AS 102

Measurement of cash-settled awards

Currently, Ind AS 102 does not provide guidance on the impact of market conditions and other vesting conditions on the number of cash settled awards to be included in the measurement of the liability (as is the case for equity settled share-based payment transactions), or on the measurement of the fair value of the liability incurred in a cash-settled share-based payment transaction.

The amendment clarifies that while computing the number of awards to be included in the measurement of the liability arising from the transaction, the best available estimate of the number of awards expected to vest would be considered and re-estimated on a periodical basis (where necessary). Vesting conditions, other than market conditions would be taken into account while adjusting these number of awards

Market and non-vesting conditions would be considered in measuring the fair value of the cash settled share-based payment transactions.

The new requirements, however, do not change the cumulative amount of expense that is ultimately recognised, because the total consideration for a cash-settled share-based payment is still equal to the cash paid on settlement. [1]

Classification of awards settled net of tax withholdings

An entity may be required to collect or withhold an amount for an employee's tax obligation on a share-based payment transaction (or withhold a portion of the shares equal to the value of the employee's tax obligation from the shares that would have been issued to the employee on vesting) and make this payment to the tax authorities on the employee's behalf. This is known as a 'net settlement feature' in the share-based payment arrangement. Currently, Ind AS 102 is unclear on whether the portion withheld should be recognised as an equity-settled or a cash-settled component.

The amendment has introduced an exception stating that, for classification purposes, a share-based payment transaction with employees is accounted for as equity-settled if:

- The terms of the arrangement permit or require a company to settle the transaction net by withholding a specified portion of the equity instruments to meet the statutory tax withholding requirement (the net settlement feature) and
- The entire share-based payment transaction would otherwise be classified as equity-settled in the absence of the net settlement feature.

The exception does not apply to equity instruments that the company withholds in excess of the employee's tax obligation associated with the share-based payment or where there is no statutory tax withholding requirement.[1]

The shares withheld in respect of the employee's tax obligation associated with the share-based payment would be accounted for as a deduction from equity, except to the extent that the payment exceeds the fair value at the net settlement date of the equity instruments withheld, in which case, the excess amount would be recognised as an expense.

The accounting treatment prescribed above is illustrated with the help of the following example based on the guidance provided by IASB in the amendments to IFRS 2:

Company A is located in jurisdiction X. The tax law of that jurisdiction requires an entity to withhold an amount for an employee's tax obligation associated with a share-based payment and transfer that amount in cash to the tax authority on the employee's behalf.

On 1 April 2017, Company A granted an award of 100 shares to an employee. That award is conditional upon the completion of four years' service. The entity expects that the employee will complete the service period.

The terms and conditions of the share-based payment arrangement have a net settlement feature. Accordingly, the entity settles the transaction on a net basis by withholding the number of shares with a fair value equal to the monetary value of the employee's tax obligation and issuing the remaining shares to the employee on completion of the vesting period.

The employee's tax obligation associated with the award is calculated based on the fair value of the shares on the vesting date. The employee's applicable tax rate is 40 per cent. The fair value of the shares on the grant date is INR2 per share and on the vesting date (i.e. 31 March 2021 is INR10 per share).

Amendments to Ind AS 102 (cont.)

Application of requirements

The computation of the fair value of shares and tax obligation is as given in the table below:

Particulars	Details
Fair value of shares on grant date	INR2* 100 shares = INR200
Fair value of shares on vesting date	INR10* 100 shares = INR1,000
Employee's tax obligation	INR1,000*40 per cent = INR400
Number of shares to be withheld and issued	INR400/INR10 per share, i.e. 40 shares will be withheld and 60 shares will be issued

The entity pays the fair value of the withheld shares in cash to the tax authority on the employee's behalf. In other words, it is as if the entity had issued all 100 vested shares to the employee, and at the same time, repurchased 40 shares at their fair value.

Particulars	Dr/ Cr	Debit (INR)	Credit (INR)
Accumulation of compensation			
Accumulated compensation expense to be recognised over the vesting period of four years based on fair value of shares at grant date			
Expense	Dr	200	
Equity	Cr		200
Recognition of liability to pay tax authorities based on fair value of shares withheld at vesting date[(a)]			
Equity	Dr	400	
Liability	Cr		400
Settlement of tax obligation			
Cash paid to the tax authority on the employees behalf at the date of settlement			
Liability	Dr	400	
Cash	Cr		400

[(a)] *The entity may consider disclosing an estimate of the amount that it expects to transfer to the tax authority at the end of each reporting period. The entity may make such disclosure when it determines that this information is necessary to inform users about the future cash flow effects associated with the share-based payment.*

(Source: Classification and Measurement of Share-based Payment Transactions, Amendments to IFRS 2 issued by IASB, June 2016)

Modification of a share-based payment transaction from cash-settled to equity-settled

There is no specific guidance in Ind AS 102 that addresses the accounting when a share-based payment is modified from cash-settled to equity-settled. The amendment clarifies that, if the terms and conditions of a cash-settled share-based payment transaction are modified, with the result that it becomes an equity-settled share-based payment transaction, the transaction is accounted for as an equity-settled transaction from the date of the modification. Companies are to apply the following approach:

- At the modification date:
  - The liability for the original cash-settled share-based payment is de-recognised
  - The equity-settled share-based payment is measured by reference to the fair value of the equity instruments granted as at the modification date, and recognised in equity to the extent that goods or services have been received up to that date, and
- The difference between the carrying amount of the liability de-recognised as at the modification date, and the amount recognised in equity as at that date, is recognised in profit or loss immediately.[1]

The accounting treatment prescribed above is illustrated with the help of the following example based on the guidance provided in the amendments to IFRS 2:

On 1 April 2017, company A grants 100 share appreciation rights (SARs) that will be settled in cash to each of its 100 employees on the condition that employees will remain employed for the next four years.

The estimated fair value of the SARs as on the below dates is:

Year	Fair value per SAR (in INR)	Total fair value (INR in crores)
31 March 2018	10	100,000
31 March 2019	12	120,000

On 31 March 2019, the entity cancels the SARs and in their place, grants 100 share options to each employee on the condition that each employee remain in its employment for the next two years. Therefore, the original vesting period is not changed. On this date, the fair value of the options is estimated at INR13.20 each.

All employees are expected to and ultimately do provide the required service.

(Source: Classification and Measurement of Share-based Payment Transactions, Amendments to IFRS 2 issued by IASB, June 2016)

Amendments to Ind AS 102 (cont.)

Application of requirements

The accounting for the share-based payment for the SARs would be:

Year	Calculation	Dr Expense (INR)	Cumulative expense (INR)	Cr Equity (INR)	Cr Liability (INR)
2017-18	100 employees*100 SARs*INR 10*1/4 (period of service provided)	25,000	25,000	-	25,000
2018-19	Re-measurement before the modification 100 employees*100 SARs*INR 12*2/4 (period of service provided) – 25,000 (expense already booked)	35,000	60,000	-	35,000

At the modification date (31 March 2019), company A applies paragraph B44A, accordingly:

- From the date of the modification, the share options are measured by reference to their modification-date fair value and, at the modification date, the share options are recognized in equity to the extent to which the employees have rendered services
- The liability for the SARs is derecognised at the modification date and
- The difference between the carrying amount of the liability derecognised and the equity amount recognised at the modification date is recognised immediately in profit or loss.

In this example, the entity compares the fair value of the equity-settled replacement award for services provided through to the modification date (INR 132,000*2/4 = 66,000) with the fair value for the cash-settled original award for those services (INR 120,000*2/4 = 60,000). The difference (INR 6,000) is recognised immediately in profit or loss at the date of modification.

The remainder of the equity-settled share-based payment (measured at its modification-date fair value) is recognised in profit or loss over the remaining two-year vesting period from the date of the modification.

Year	Calculation	Dr Expense (INR)	Cumulative expense (INR)	Cr Equity (INR)	Cr Liability (INR)
2018-19	Balances carried forward	-	60,000	-	60,000
2018-19	De-recognition of the liability, recognition of the modification date fair value amount in equity and recognition of the effect of settlement for INR6,000	6,000	66,000	66,000	(60,000)
2019-20	100 employees*100 share options*INR13.2*3/4 (period of service provided) – INR66,000 (expense already recognised)	33,000	99,000	33,000	-
2020-21	100 employees*100 share options*INR13.2*4/4 (period of service provided) – INR99,000 (expense already recognised)	33,000	132,000	33,000	-
	Total			132,000	-

(Source: Classification and Measurement of Share-based Payment Transactions, Amendments to IFRS 2 issued by IASB, June 2016)

Effective date and transition

The amendments are effective for annual periods beginning on or after 1 April 2017. The amendments can be applied prospectively so that prior periods do not have to be re-stated. Retrospective application is permitted, provided companies have the required information.

Amendments to Ind AS 7

Liabilities arising from financing activities are liabilities for which cash flows were, or future cash flows will be classified in the statement of cash flows as cash flows from financing activities. To enable users of financial statements to evaluate changes in liabilities arising from financing activities, the amendment requires entities to disclose changes arising thereon from non-cash transactions in addition to changes from financing cash flows. These changes may include:

- Changes arising from obtaining or losing control of subsidiaries or other businesses
- The effect of changes in foreign exchange rates
- Changes in fair values and
- Other changes.

Additionally, the disclosure also applies to changes in financial assets (for example, assets that hedge liabilities arising from financing activities) if cash flows from those financial assets were, or future cash flows will be, included in cash flows from financing activities.

Disclosures

Entities may provide a reconciliation between the opening and closing balances in the balance sheet for liabilities and financial assets arising from financing activities. While providing such disclosures, the entity should:

- Provide sufficient information to enable users of the financial statements to link items included in the reconciliation to the balance sheet and the statement of cash flows and
- Where the entity provides this disclosure in combination with disclosure of changes in other assets and liabilities, it should disclose the changes in liabilities and financial assets arising from financing activities separately from changes in those other assets and liabilities.

The illustrative examples accompanying IAS 7 issued by the IASB illustrate one possible way of presenting this disclosure in the format below:

	20X1	Cash flows	Non-cash changes			20X2
			Acquisition	Foreign exchange movement	Fair value changes	
Long-term borrowings	22,000	(1,000)	-	-	-	21,000
Short-term borrowings	10,000	(500)	-	200	-	9,700
Lease liabilities	4,000	(800)	300	-	-	3,500
Assets held to hedge long-term borrowings	(675)	150	-	-	(25)	(550)
Total liabilities from financing activities	35,325	(2,150)	300	200	(25)	33,650

(Source: Disclosure Initiative, Amendments to IAS 7 issued by IASB, January 2016)

Effective date and transition

The amendments are effective for annual periods beginning on or after 1 April 2017. When the entity first applies these amendments, it is not required to provide comparative information for preceding periods.

Our comments

The amendments to Ind AS 102 and Ind AS 7 are in line with amendments made to IFRS and are designed to improve the practical application of these standards. Companies that have transitioned to Ind AS or are in the process of implementing Ind AS should carefully consider the impact of the revised guidance in preparing their financial information for periods beginning on or after 1 April 2017. While the amendments do not explicitly permit early adoption, entities may consider if early adoption would result in presentation of more relevant and useful financial information.

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The website provides information and resources to help board and audit committee members, executives, management, stakeholders and government representatives gain insight and access to thought leadership publications that are based on the evolving global financial reporting framework.

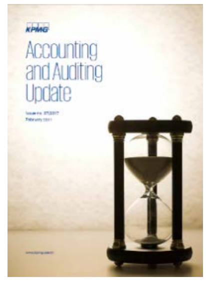
Voices on Reporting

KPMG in India is pleased to present Voices on Reporting – a monthly series of knowledge sharing calls to discuss current and emerging issues relating to financial reporting.

Special session on FAQs on ICDS issued by CBDT

In our recent call, we provided an overview and implications of the clarifications provided by CBDT on issues relating to application of ICDS. These clarifications were provided by CBDT in the form of Frequently Asked Questions (FAQs) issued on 23 March 2017.

Missed an issue of our Accounting and Auditing Update or First Notes



Issue no. 7/2017 – February 2017

Continuing with our series of articles on the revised requirements of the Companies Act, 2013 (2013 Act), this month's edition of the Accounting and Auditing Update (AAU) carries an article on the Consolidated Financial Statements (CFS). The article provides an overview of the revised requirements relating to CFS under the 2013 Act and Securities and Exchange Board of India regulations.

Our article also explains impacts of the CFS on accounting of deferred taxes of a group in relation to intra-group transactions and undistributed profits of a subsidiary, associate and joint venture.

Our article on the Insolvency and Bankruptcy Code (Code) provides an overview of the requirements and implications of the Code.

Additionally, this publication carries an article explaining the accounting of debt for equity swap with help of illustrative examples and flowcharts.

Our article also highlights key differences in accounting of oil and gas producing activities under the guidance note issued by ICAI under Indian GAAP vis-à-vis guidance note issued by ICAI under accounting framework of Ind AS.

The publication also carries regular round up of regulatory updates in India and internationally.

CBDT issues FAQs on ICDS

28 March 2017

On 31 March 2015, the Ministry of Finance (MoF) issued 10 Income Computation and Disclosure Standards (ICDS) operationalising a new framework for computation of taxable income by all assessees in relation to their income under the heads 'Profit and gains of business or profession' (PGBP) and 'Income from other sources'. The ICDS are applicable to the specified assessees from Assessment Year (AY) 2017-18.
However, certain changes have been made to them. They are:

- Revised ICDS issued
- Revised Tax Audit Report (Form No. 3CD)
- MAT computation formulae for Ind AS companies

The CBDT received a number of queries on various aspects of ICDS. Therefore, on 23 March 2017, CBDT issued clarifications in the form of Frequently Asked Questions (FAQs) on issues relating to the application of ICDS.

This issue of First Notes provides an overview of the responses issued by the CBDT corresponding to the ICDS related issues raised.

Previous editions are available to download from: www.kpmg.com/in