Indian Accounting Standards and Transfer Pricing

Discussion paper

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Background

1.1. The Ministry of Corporate Affairs (MCA) on 16 February 2015 issued Ind AS (Indian Accounting Standards) comprising 40 accounting standards that are largely in line with International Financial Reporting Standards (IFRS).[1] As a result certain Indian companies were required to draw up their financial statements starting with quarterly results for Financial Year (FY) 2016-17 based on Ind AS.

1.2. Ind AS introduces significant differences from the requirements of existing Indian Generally Accepted Accounting Principles (AS) in areas such as revenue recognition, property, plant and equipment, financial instruments, business combinations, consolidation, etc. In addition to changes in the requirements of the standards themselves, there are several areas where Ind AS requires application of judgement and financial reporting would be based on estimates made by the management.

1.3. Further, there are certain significant deviations from IFRS which have been made optional to facilitate a smooth transition from AS to Ind AS. For example, under Ind AS companies have the choice of using the carrying value of property, plant and equipment as of 1 April 2015 under AS as the deemed cost.

1.4. The MCA has laid down a road map in phases for companies (other than banks, insurance companies and non-banking financial companies) based on net worth for applicability of Ind AS tabulated below:

Phase	Effective date	Applicability
I	1 April 2016 (with 1 April 2015 as the transition date[2])	Applicable if net worth >= INR500 crore[3]
II	1 April 2017 (with 1 April 2016 as the transition date)	Applicable if net worth >= INR250 crore[4] (unlisted companies) Applicable to all remaining listed companies[5]

1.5. Separate road maps have been issued for banks, insurance companies and non-banking financial companies with the first cycle of applicability from 1 April 2018 onwards (transition date 1 April 2017).

1.6. Based on the road map for corporates, listed companies with a net worth of INR500 crore or more were required to report their results for the quarter ended 30 June 2016 as per the requirements of Ind AS. This would mean that from the financial year 2016 -17 onwards companies in India will be split into two groups from a financial reporting perspective, large companies who would be preparing financial statements per the requirements of Ind AS and other companies which would continue preparing their financial statements as per requirements of AS.

1.7. As of 30 May 2017, 38 companies listed on the Nifty 50 were required to publish their accounts as per Ind AS, for the year ended 31 March 2017. The impact of the transition to Ind AS on performance measures such as revenue, earnings before interest, taxes, depreciation and amortisation (EBITDA), interest, tax, PAT, depreciation and net worth, have been shown below, which portrays an increase/ decrease in the performance measures.

1. The Government of India in consultation with the Institute of Chartered Accountants of India decided to converge and not to adopt IFRS. There are several differences between Ind AS and IFRS, known as carve-outs.
2. The transition date denotes that comparative Ind AS numbers for FY 15-16 would be provided in the Ind AS financials for FY 16-17.
3. Holding, subsidiary, joint venture or associate companies of companies covered.
4. Ibid
5. Ibid

Revenue	EBITDA	Interest	Tax	PAT	Depreciation	Net worth
▲ 4.0%	▼ 3.3%	▲ 4.0%	▼ 1.6%	▲ 2.0%	▼ 8.6%	▲ 8.8%

	Revenue		EBITDA		Interest		Tax		PAT		Depreciation	
	No. of cos.	% Change	No. of cos.	% Change	No. of cos.	% Change	No. of cos.	% Change	No. of cos.	% Change	No. of cos.	% Change
Total change	38	4%	21	(3.3)%	38	4%	38	(1.6)%	38	2.0%	38	(8.6)%
Companies with increase	22	8.2%	15	3.6%	25	21.4%	15	5.7%	17	10.9%	10	6.9%
Companies with no change	2	0.0%	0	0.0%	1	0.0%	0	0.0%	0	0.0%	1	0.0%
Companies with decrease	14	(7.0)%	23	(6.7)%	12	(16.4)%	23	(8.4)%	21	(4.0)%	27	(12.5)%

Source: Ind AS - Practical perspectives (Q4-4-June), KPMG in India, 2017

1.8. This difference in the fundamental accounting methodology applicable to companies is likely to pose various challenges from a transfer pricing perspective. We capture the various issues resulting from the differences in accounting principles by transitioning to Ind AS from existing AS in the next section.

Issues involved

2.1 Benchmarking and reporting

A. Determination of arm's length margin

2.1.1. In determining the arm's length price from a transfer pricing perspective, a taxpayer is required to employ the methods as prescribed in Section 92C of the Income-tax Act, 1961 (the Act). These methods are: Comparable Uncontrolled Price Method (CUP), Resale Price Method (RPM), Cost Plus Method (CPM), Profit Split Method (PSM), Transactional Net Margin Method (TNMM) and Other Method.

2.1.2. The RPM, CPM, and TNMM being profit based methods, rely on Profit Level Indicators (PLI) as a measure of profitability earned by companies. PLIs used may inter alia be Operating Margin (Operating Profit/Sales), Net Cost Plus (Operating Profit/Total cost), Gross Margin (Gross Profit to Sales), Berry Ratio (Gross Profit to Operating Expenses). The comparison of PLIs may be based on internal or external comparables.

2.1.3. When applying the above methods using external comparables, a set of comparable companies is arrived at from publicly available databases and margins computed based on publicly disclosed accounting information of these entities. Since the implementation of Ind AS is being done in phases, having companies following two different financial reporting frameworks will pose significant challenges due to differences in company results. For instance, employee share based payments are accounted on fair value under Ind AS whereas under AS, they are recognised based on intrinsic value. Share based compensation directly affects the operating costs of a company and may therefore affect the calculation of the PLI that include costs. The details of the differences between the existing and the new accounting standards have been discussed in Annexure 1.

2.1.4. The differences are likely to impact the single year margins as well as the multiple year margins. In a case where single year margins are used, it may so happen that certain comparable companies are following AS and certain comparable companies are following Ind AS. We have analysed certain widely used sets of comparable companies (listed and unlisted) for various activities such as IT, ITeS, marketing support services, etc. and observed that for FY 2017 and FY 2018 approximately 16 per cent and 62 per cent of the comparables would transition to Ind AS in year one and two respectively.

2.1.5. Where multiple years are used for transfer pricing analysis, a situation may arise in Year one whereby the financial information for a comparable which has transitioned to Ind AS in Year one would be drawn up as per Ind AS for FY 2016-17, and for FY 2014-2015 and FY 2015-16 as per AS. This may not reflect an accurate picture of the three-year weighted average profits of the said comparable company.

2.1.6. As a result of the above differences, the range worked out based on results of companies following accounting standards under AS and Ind AS without adjustments may not reflect the correct range/arm's length price. Hence, the implications of the convergence process on transfer pricing planning and analysis needs to be examined and appropriate steps have to be taken to minimise the differences arising due to the same.

2.1.7. Considering the above areas of impact of transition to Ind AS on transfer pricing, it becomes imperative to examine the need for adjustments in order to harmonise the results of comparable companies and tested party to ensure robust comparability.

2.1.8. Further, companies which have adopted Ind AS, would require adjustments to be made to align the Ind AS numbers with AS.[6] This is because majority of the companies (listed and unlisted) are following AS. This is based on a review of data publically available for companies, where we observed that for FY 2017 and FY 2018 approximately 98 per cent and 80 per cent of the companies would continue to follow AS. In this regard, the position on adjustments remains the same as described in Annexure 1. Further, based on facts of each case, we may understand from the taxpayer major impact areas and assess the need for adjustments.

6. Please refer to Annexure 2 for the mapping of Accounting Standards under Ind AS with AS; Accounting Standards that do not have any impact on transfer pricing benchmarking analysis are outlined in Annexure 3 and Accounting Standards that have an impact on transfer pricing benchmarking analysis are outlined in Annexure 4.

B. Working capital adjustment

2.1.9. Working capital adjustment for difference in level of working capital between tested party and comparables is measured against the sales and operating cost numbers of tested party and comparables. Hence, there is a need to adjust the sales and cost numbers for differences arising due to a separate set of accounting standards followed by tested party and comparables while transitioning to Ind AS.

C. Application of filters

2.1.10. While conducting searches on public databases, certain filters are applied such as exclusion of companies with say sales less than INR1 crore or sales of more than INR200 crore, manufacturing/trading sales to total sales, service income to total sales, advertising, marketing and distribution expenses to total sales, research and development expense to total sales, export income to total sales, employee cost to total sales/total cost, related party filter, which are all based on the profit and loss (P&L) data. There could be differences in revenue, profit, fixed assets values for companies following Ind AS vis-à-vis companies following AS. This may impact the universe of companies selected for further analysis.

D. Need for adjustments

2.1.11. An analysis of the key differences in the Accounting Standards under AS and Ind AS are tabulated in Annexure 1. It is observed that certain differences between Ind AS and AS would merit adjustments. However, there could be a potential challenge in making adjustments for certain differences due to lack of adequate disclosures in the year of transition to Ind AS and subsequent years.

2.1.12. All the differences between Ind AS and AS may not be possible to adjust and there is a certain amount of subjectivity and assumptions required to be made in working out the adjustments.

2.1.13. Certain adjustments may have a material impact on the margins of a company while some may not have a material impact. Considering this, one could make the adjustments to the best extent possible, which will reduce the differences between the accounting standards to a certain extent. Some of the key adjustments that could be considered are as follows:

- Adjustment to fair value plant, property and equipment (PP&E);
- Adjustment for revenue recognition in relation to cash discounts and incentives;
- Adjustment for actuarial gain/losses in relation to employee benefits;
- Adjustment for share based payment.

2.1.14. However, due to the difficulty in making reliable adjustments for all differences each case would need to be reviewed separately and the need for adjustments be reviewed individually. This is in line with the practice adopted by various countries internationally while transitioning to IFRS. Further, even under the AS there could have been different positions adopted by taxpayers from an accounting perspective which were not adjusted. The impact of such differences may get evened out by using a range worked out on the basis of thirty-fifth and sixty-fifth percentile, as prescribed under the Indian Transfer Pricing legislation.

E. Reporting

2.1.15. For a company that adopts Ind AS, reporting in Form 3CEB should be as per Ind AS financial statements. Any change in accounting in relation to Ind AS, including components of the transactions may need to be understood and documented.

2.1.16. Further, under AS, control was considered to be established based on control over more than one half of voting rights and/or control over the composition of the board of directors. This would be the case even if there may be a joint venture agreement in place where control over operations has been agreed to be exercised jointly.

2.1.17. Under Ind AS, while ownership of voting rights and control of composition of board of directors are required to be considered while evaluating control, reporting entities are also required to consider contractual arrangements, etc. as part of the evaluation. Control is considered to exist when the reporting entity has control over all relevant activities of the investee. Similarly, in certain cases, companies may be identified as subsidiaries even in cases where the reporting entity owns less than one half of the voting rights. Based on the above, the related party disclosures may undergo a change considering the wider definition of control under Ind AS. Hence, it is important that the interplay between Ind AS and transfer pricing for the purpose of reporting of Associated Enterprises be evaluated. Further, in cases where reporting entities use a value other than transaction values for the purposes of Ind AS financial statements, the values to be used for related party disclosures may need to be evaluated.

2.2 Financial instruments

A. Redeemable preference shares/ perpetual debenture/compulsorily convertible debenture

2.2.1 A new Section in the Act, Section 94B, has been introduced relating to limitation of interest deduction in certain cases. This section provides that interest paid by an Indian Company or a permanent establishment of a foreign company in India to its Associated Enterprises (AE), shall be restricted to 30 per cent of EBITDA of the borrower, or interest paid or payable to the AE, whichever is less.

2.2.2 In this regard, it is relevant to note that under AS, redeemable preference capital is treated as equity whereas under Ind AS redeemable preference shares are classified as debt and the dividend is treated as interest cost. Further, depending on the terms and conditions, generally perpetual debentures/ compulsorily convertible debentures in certain situations are accounted as equity under Ind AS in relation to loan classification under AS. Optionally convertible debentures/bonds are also generally required to be accounted for as a separate liability and equity components.

2.2.3 The question which emerges from the above discussion is whether change in characterisation of an instrument from an accounting perspective would impact the treatment given for deduction of interest for calculating taxable profits and be subject to the limitation of interest deduction as per Section 94B of the Act.

2.2.4 Further, General Anti-Avoidance Rules (GAAR) have been introduced in the Act with effect from financial year 2017-18 by including a new Chapter XA. As per GAAR, the revenue authorities may declare an arrangement as an 'impermissible avoidance arrangement' if the main purpose of the arrangement is to obtain a 'tax benefit' and the arrangement lacks or is deemed to lack commercial substance. In this context, it needs to be seen whether the re-characterisation of transaction from an Ind AS perspective may lead to scrutiny by the revenue authorities on the commercial substance of the transaction.

B. Guarantee

2.2.5 Under Ind AS, if a parent issues a corporate guarantee on behalf of a subsidiary/associate/ joint venture, the parent is required to report a notional guarantee income with a corresponding impact on the investment in the respective entity. The notional guarantee income is determined with reference to the guarantee commission which a third party would have charged in an arm's length arrangement.

2.2.6 Indian parent companies issuing guarantees so far have been in certain cases adopting a position that no guarantee fee is chargeable on a guarantee provided to a group company, based on the premise that the guarantee provided is in the nature of a shareholder activity. The courts have further upheld this position based on the premise that there is no impact on profits, income, losses or assets of the parent. The reporting of notional guarantee income in the books of guarantor on transitioning to Ind AS would now have an impact on profits and hence there would be a mis-match in the position adopted by an entity for tax and accounting purposes. This could result in a potential challenge in justifying the position adopted by the taxpayers before the tax authorities.

2.2.7 If a sum is disclosed as guarantee fee in the financial statements, the revenue authorities may seek to make an adjustment equivalent to at least the amount of guarantee fee disclosed in the Ind AS financials. Hence, it is important to harmonise the positions being adopted for tax and accounting purposes.

C. Loans

Interest free loans/concessional interest bearing loans

2.2.8 Under Ind AS, if a parent company provides an interest free/concessional interest bearing loan to its subsidiary/associate/joint venture, such loans are required to be measured at fair value on initial recognition in the books of the parent/investee and the difference may be reflected as deemed investment (by the parent) and deemed capital contribution (by the investee). Both the parent and the investee would thereafter be required to reflect notional interest income/expense with reference to the discounting rate used for determining fair value on initial recognition.

2.2.9 In light of the above, advancing interest free loans to related parties generally on the pretext of commercial expediency may now be exposed to higher litigation, as notional income on all such loans will now be reported in the books of accounts based on fair value.

2.2.10 Further, in relation to concessional interest bearing loans, the amount of interest reported in the books of accounts will be as per fair value. Hence, the revenue authorities could equate the amount reported in the books of accounts to be the arm's length interest. It would therefore be important to maintain adequate rationale to justify the concessional interest rate charged.

2.2.11 In light of this information, it would once again be important to harmonise the position adopted from a tax and accounting perspective.

Interest rate benchmark

2.2.12 For interest rate benchmarks as a starting point, we calculate the credit rating of the borrower. This credit rating is based on certain P&L and balance sheet line items which help arrive at the credit worthiness of the borrower, based on which similarly rated issuances are sought to be identified and used for the purpose of determining the arm's length interest rate payable/receivable.

2.2.13 In such a case, the line items used to calculate the credit rating of the Indian borrower were based on AS financials, however the issuances selected, which were primarily foreign borrowers, had their credit ratings determined based on the accounting principles followed in their respective jurisdictions. In this sense, a 'B' rated borrower in India may not be comparable to a 'B' rated borrower in a foreign jurisdiction due to differences in the P&L and balance sheet numbers used to determine the credit rating.

2.2.14 Now that Ind AS is followed by Indian companies which is converged with IFRS, with certain deviations/carve-outs, most differences in accounting would be aligned.

2.3. Advance Pricing Agreements

2.3.1 While negotiating for Advance Pricing Agreements (APA), it would be relevant to analyse the impact of transition to Ind AS on the arm's length margins agreed in the APA, as there would be a difference in the cost base and revenue values as a result of transition to Ind AS. Say, for instance, for a distributor entity, the arm's length margin agreed in the APA is 5 per cent on sales. As a result of transitioning to Ind AS, there would be difference in sales and cost values during the rollback and APA period, as for a certain period the APA applicant would have followed AS and for certain period Ind AS, this would impact the transfer pricing agreed year on year as per the APA.

2.3.2 Therefore, one should be mindful at the time of discussions with the APA authorities to consider the changes that will impact the price agreed in the APA as a result of transitioning to Ind AS.

2.3.3 Generally, the APA authorities include a clause taking cognisance of the change in accounting methodology and have not recommended any adjustments.

2.4. Base Erosion and Profit Shifting

2.4.1 Section 286 of the Act states that a parent entity in India would have to file a Country-by-Country Report (CbyC report) for financial year 2016-17 before due date of filing of return of income if the consolidated revenue of the group in the previous year exceeds the prescribed threshold. The threshold prescribed as per the Memorandum of Finance Bill 2016 is EUR750 million. In the CbyC report a taxpayer is required to furnish *inter alia*, aggregate information in respect of the amount of revenue, profit or loss before income-tax, amount of income-tax paid, amount of income-tax accrued, stated capital, accumulated earnings, number of employees and tangible assets not being cash or cash equivalents with regard to each country in which the group operates.

2.4.2 The possible question which could arise is whether the CbyC report would be impacted as a result of transitioning to Ind AS. In this regard, a majority of the companies that will require CbyC compliance will be large companies that may also transition to Ind AS. Considering that the first year for CbyC compliance and Ind AS is FY 16-17, there should be no impact of the transition on CbyC. However, for companies required to comply with the CbyC rules, but continuing to follow the existing AS, on the date of transition to Ind AS, based on the guidance provided in 'Action 13 on Transfer Pricing Documentation and Country-by-Country Reporting' issued by OECD, a disclosure may be required to be made in Table 3 of the CbyC report which is the Additional Information section, where an explanation could be inserted for the change in Accounting Standards. The relevant para providing the guidance is reproduced below:

'Source of data
The Reporting MNE should consistently use the same sources of data from year to year in completing the template. The Reporting MNE may choose to use data from its consolidation reporting packages, from separate entity statutory financial statements, regulatory financial statements, or internal management accounts. It is not necessary to reconcile the revenue, profit and tax reporting in the template to the consolidated financial statements. If statutory financial statements are used as the basis for reporting, all amounts should be translated to the stated functional currency of the Reporting MNE at the average exchange rate for the year stated in the Additional Information section of the template. Adjustments need not be made, however, for differences in accounting principles applied from tax jurisdiction to tax jurisdiction. The Reporting MNE should provide a brief description of the sources of data used in preparing the template in the Additional Information section of the template. If a change is made in the source of data used from year to year, the Reporting MNE should explain the reasons for the change and its consequences in the Additional Information section of the template.'

2.4.3 As per existing AS, for Joint ventures (JVs), there was a line by line consolidation (proportionate to the extent of stake held) whereas under Ind AS, only share of profits of JVs are consolidated. Based on the above, it is relevant to evaluate whether JVs would be considered as constituent entities as per Ind AS.

2.5. Review of functional and economic analysis of lease versus service arrangements

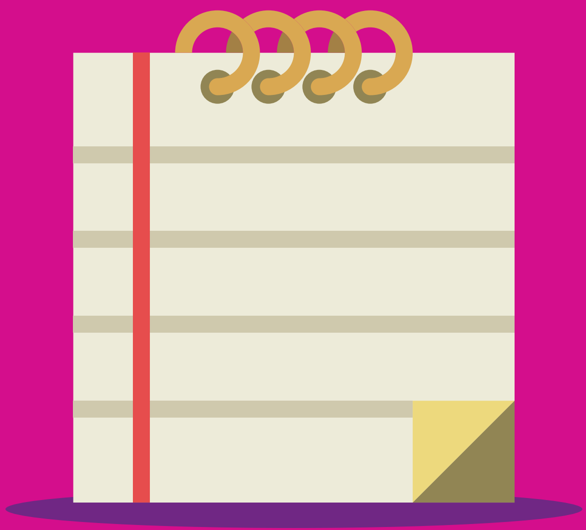
In the case of arrangements where a large part of capacity is earmarked for a specific customer, currently under AS, such arrangements are normally considered as those for providing services and not a leasing activity. In the case of Ind AS, arrangements that do not take the legal form of lease but fulfillment of which is dependent on the use of specific assets and which convey the right to use are accounted for as embedded lease. Now that such contracts for supply of goods and services may get concluded as leases, it needs to be examined whether the change in characterisation under Ind AS for such arrangements would require a review of the function, asset and risk analysis and economic analysis.

Way forward

In light of the various issues resulting due to transition to Ind AS, it is important that Indian Companies (whether following AS or Ind AS) familiarise themselves with the key differences, understand the implications of the transition to Ind AS for transfer pricing analysis and establish a system to review and address such issues. The following points merit consideration from a transfer pricing perspective:

- Need for adjustments while conducting transfer pricing benchmarking analysis using external comparables;
- Review of functional and economic analysis and intercompany agreements to reflect the substance of the transaction;
- Review of the proportion of debt and equity in the capital structure and the impact of re characterisation of financial instruments as per Ind AS from a GAAR perspective;
- Review of impact on pricing agreed in the APA as a result of transitioning to Ind AS due to change in transfer price;
- Documenting rationale for corporate guarantee with nil guarantee fee and interest free loan/concessional interest bearing loans;
- Review of constituent entities to be reported in the CbyC report;
- Evaluation of Associated Enterprise relationship from the perspective of control under Ind AS.

Annexures



Annexure 1

Key differences between Accounting Standards under AS and Ind AS and the areas of impact

Ind AS	AS	AS	Ind AS	Need for adjustments
8 Accounting Policies, Changes in Accounting Estimates and Errors	5 Net Profit or Loss for the Period, Prior Period Items and Changes in Accounting Policies	Requires the computation of the prior period items retrospectively. The cumulative impact of the rectification is disclosed in the current accounting period as a separate line item after PBT.	Requires the computation of the prior period item retrospectively. The impact of the retrospective computation is shown in the respective financial year.	Currently, under AS when computing margins, prior period items are considered as non- operating as these do not pertain to the year in which these are disclosed. Under Ind AS the prior period item is reflected in the relevant year to which it relates and hence there may not be a need to adjust for prior period item in the current year.
16 Plant, Property and Equipment (PP&E)	10 and 6 Accounting for Fixed Assets and Depreciation Accounting	Property plant and equipment are measured at historical cost.	Companies have the following choices for recognition of PP&E on the date of transition in relation to existing items of property plant and equipment: i. Previous AS carrying value as deemed cost ii. Fair value of property plant and equipment as deemed cost iii. Retrospective	There will be an impact on depreciation as PP&E is valued at fair value under option (ii) and (iii). This may merit an adjustment. If a company chooses option (i) and follows the same methodology for measuring PP&E as they did under AS, no adjustment may be required.
17 Leases	19 Leases	Does not contain any specific guidance on embedded lease and transactions/ arrangements are recorded as sale, purchase or rendering of service, based on their nature	Arrangements which are not legally structured as leases may be identified to be embedded lease arrangements if such arrangements involve a specific asset and convey a right to use the respective asset. e.g. toll manufacturing arrangements where the customer purchases 100% output from asset legally owned by the toll manufacturer and involves a minimum commitment to purchase (take or pay arrangement), may be identified as embedded lease arrangements.	From lessee's perspective - No significant impact on profitability, however there could be a change in the manner in which line items will be reported. Under Ind AS, an arrangement previously classified as an expense line item in the P&L account will now be classified as lease i.e. operating lease or finance lease. In case of a finance lease: 1. Assets are recognised by the lessee and accordingly, depreciation is charged on it. 2. There will also be a finance lease obligation in the form of interest on lease. The value of expenses as charged in finance lease i.e. depreciation and interest may be similar to the expense charged under AS, and will be disclosed separately. In case of an operating lease: Instead of classifying the transaction as an expense, it will get classified as lease rental. From Lessor's perspective - Impact on Revenue. Under Ind AS, an arrangement previously classified as income from operations in the P&L account will now be classified as lease i.e. operating lease or finance lease. In case of a finance lease: 1. Assets are derecogonised by the lessor and accordingly, the related depreciation will have to be reversed. 2. There will instead be a finance lease receivable in the form of interest on lease. The amount of income recognised under finance lease i.e. interest income may be similar to the amount net of rent income and depreciation expense recognised under AS and hence there may be no significant impact on the profitability. In case of an operating lease: Instead of classifying the transaction under revenue from operations, it will get classified as lease income. Since rental income is considered as operating, no adjustment may be made.

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Annexure 1

Key differences between Accounting Standards under AS and Ind AS and the areas of impact

Ind AS	AS	AS	Ind AS	Need for adjustments
		Lease deposits are reported at their transaction value.	All financial assets and liabilities to be valued at fair value and hence the initial difference between the transaction value and fair value of the lease deposit be treated as prepaid rentals. This amount would be recorded in the profit and loss account on a straight line basis over the lease term with the unwinding of discounting impact as interest income	Under Ind AS the difference between the fair value and transaction value will be amortised over the period of the lease and may be disclosed as rent expense. In addition, interest income may be recognised over the period as well. In such a case, to align Ind AS to AS from the lessee's and lessors perspective an adjustment may need to be made.
		Lease rentals under an operating lease should be recognised as an expense in Profit and Loss statement on a straight line basis.	There is a carve out in Ind AS for not straight lining lease rentals if the escalation of rentals is in line with the expected general inflation. In such a case, the actual amount related to a particular period will be debited in that period itself.	There could be a challenge in making adjustment in the absence of adequate disclosures
18 Revenue	9 Revenue	When a company operates on custom, insurance and freight (CIF) basis, generally revenue is recognised on dispatch basis to the ultimate customer.	Where the terms of the contract cast the responsibility of freight and insurance on the seller, the revenue is permitted to be recognised only on delivery to the ultimate customer.	There would be difference in the revenue reported by companies under Ind AS in relation to AS, however at the same time there would be a corresponding timing difference in the cost. Therefore there should be no impact on the operating ratios.
		Revenue is recognised at the contractual value of the consideration receivable	Measurement of revenue at fair value of the consideration receivable. If the company offers an extended credit period (generally material if greater than one year) to customers, revenue is recognised at the present value of future cash inflows. Interest income is recognised over the credit period for the difference between the revenue recognised and the stated transaction value.	There could be a challenge in making appropriate adjustment as no separate disclosure is available to make adjustments. However, extended credit period for more than one year is rare in a normal business scenario and may generally arise in certain cases of retention money in relation to construction and other engineering, procurement and construction contracts.
		Cash discounts and incentives are presented as an expenditure.	All discounts and incentives (which are linked to the volume of sales) are required to be presented as a reduction from revenue. However other sales promotion expenses such as advertisement expense, etc. are shown separately as expenses.	There would be a difference in the revenue recognised by companies that follow Ind AS, as revenue would be reduced to the extent of cash discounts and incentives which were previously disclosed as a sales promotion expenditure under AS. Hence, an adjustment would be required to be made for the differences outlined.
		Excise duty is presented as a reduction from revenue.	Excise duty has to be presented on a gross basis i.e. as an expenditure in the income statement.	An adjustment may be considered in order to align the revenue numbers.

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Key differences between Accounting Standards under AS and Ind AS and the areas of impact

Ind AS	AS	AS	Ind AS	Need for adjustments
18 Revenue	9 Revenue	Multiple arrangement (e.g. a company sells a phone along with free talk time for a certain period. The cost of the talk time is generally built in to the cost of the phone. These are two transactions shown as one) There is no specific guidance provided under AS on multiple element arrangement. In absence of specific guidance, practice varies. Generally revenue is not split and only an estimated liability for redemption of goods or services is recorded.	The revenue recognition criteria are usually applied separately to each transaction. However, in certain circumstances, it is necessary to separate a transaction into identifiable components (certain components will be recognised only when utilised and not on an upfront basis) in order to reflect the substance of the transaction. At the same time, two or more transactions may need to be grouped together when they are linked in such a way that the whole commercial effect cannot be understood without reference to the series of transactions as a whole. The price that is regularly charged when an item is sold separately is the best evidence of the item's fair value. At the same time, under certain circumstances, a cost plus reasonable margin approach to estimating fair value would be appropriate under Ind AS	An adjustment maybe considered in order to align revenue numbers.
19 Employee Benefits	15 Employee Benefits	Actuarial gains/losses are recognised in the Statement of Profit and Loss in the period in which they arise.	Actuarial gains/losses are recognised entirely in the reserves.	An adjustment may be considered based on the disclosures made in the financial statements.
20 Accounting for government grants and disclosure of government assistance	12 Accounting for government grants	Grants relating to fixed assets are permitted either to be reduced from the related fixed asset or presented as deferred government grant on the balance sheet.	Only the gross approach is permitted i.e. capital grants are not permitted to be reduced from the related fixed asset.	An adjustment would be required to bring the Ind AS numbers to be in line with AS as some companies follow the first approach under AS of disclosing fixed asset by reducing the value of government grants.
21 The Effects of Changes in Foreign Exchange Rates	11 The Effects of Changes in Foreign Exchange Rates	Companies are permitted to capatalise foreign exchange fluctuation to fixed assets or recognise the fluctuation in reserves (and amortise over the tenure of the related borrowing).	For new borrowings raised after 1 April 2016 (for phase 1 companies) foreign exchange fluctuation is required to be recognised as an expense in the period in which such fluctuation arises. Further, with respect to borrowings raised prior to 1 April 2016, companies have a choice to continue with AS policy of capitalisation of the fluctuation or can change the accounting policy and recognise the same in the income statement.	Under Ind AS disclosure of the amount of fluctuation in relation to the long-term borrowings will be made available in the interest income/expense schedule. As interest is non-operating in nature, no adjustment should be required. However, if the company under AS has capitalised the foreign exchange fluctuation, it would impact the depreciation charged to the P&L and hence adjustment may be required to the extent of the impact of forex fluctuation on depreciation recorded as per AS.
37 Provisions, Contingent Liabilities and Contingent Assets	29 Provisions, Contingent Liabilities and Contingent Assets	The provisions are recognised at their expected value without an adjustments for time value of money	Discounting the amounts of provisions, if effect of the time value of money is material.	An adjustment would be required to be made for the differences outlined.

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Annexure 1

Key differences between Accounting Standards under AS and Ind AS and the areas of impact

Ind AS	AS	AS	Ind AS	Need for adjustments
38 Intangible Assets	29 Intangible Assets	No such provision.	In case of an acquisition of intangibles, payment deferred beyond normal credit terms should be recognised as interest expense over the period of credit unless it is capitalised.	Challenge in making appropriate adjustment, as there will be no separate disclosure of the actual cost of asset including time value for money.
		No such provision.	In case of disposal of intangibles, if payment of consideration on disposal of intangible asset is deferred, consideration recognised is cash price equivalent.	This would have an impact on the P&L which is non-operating in nature. Hence, it needs to be ascertained if an adjustment would be required.
		Under AS, all intangible assets are mandatorily required to be amortised over the expected useful life.	Under Ind AS, intangible assets with indefinite useful lives need not be amortised and are required to be tested for impairment on an annual basis.	Adjustment maybe required.
102 Share based payment	Guidance note on accounting for employee share based payments	Share based payments (ESOPs) are measured with reference to their intrinsic value i.e. difference between market price of the shares on the date of grant and the exercise price.	ESOPs are required to be measured at fair value determined with reference to the Black Scholes model or binomial model. Further, expenses in relation ESOPs with a graded vesting feature are required to be recognised on an accelerated basis.	The difference of the stock compensation under fair value method and intrinsic value method should be adjusted to align the AS number with Ind AS.
109 Financial Instruments	13 Accounting for Investments	Companies were required to recognise unrealised losses on short-term investments and derivatives but not unrealised gains.	All equity instruments (other than those which are in relation to subsidiaries, associates and joint ventures), all other trading investments (e.g. investment in debt securities), all derivatives are required to be measured at fair value through profit or loss i.e. unrealised gains are also required to be recognised on such instruments.	An adjustment would be required to be made for the differences outlined.
		Companies make provision for customers who are identified as impaired using either an ageing based approach or specific individual assessment.	Companies are required to recognise provision for bad and doubtful debts with reference to an expected credit loss model approach i.e. in addition to provision for customers who are identified as impaired. Reporting entities are also required to provide for customers who are expected to default in future periods. This is determined with reference to the past trend/history as applicable to the respective reporting entity. This provision is made at the time of sale.	The difference for the provision of doubtful debts will be available and adjusted in reserves at the point of transition i.e. for April 2015. There will be no separate disclosure detailing how the provision is made year on year, considering it is an estimate and hence there is a challenge in making adjustment.

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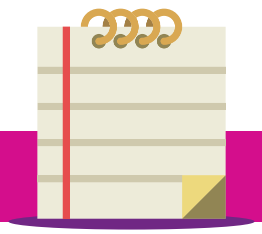
Annexure 2

Mapping of Ind AS and AS[7]

Title of Ind AS	Ind AS	AS
Presentation of Financial Statements	1	1
Inventories	2	2
Statement of Cash Flows	7	3
Accounting Policies, Changes in Accounting Estimates and Errors	8	5
Events after the Reporting Period	10	4
Construction Contracts	11	7
Income Taxes	12	22
Property, Plant and Equipment	16	6, 10
Leases	17	19
Revenue	18	9
Employee Benefits	19	15
Accounting for Government Grants and Disclosure of Government Assistance	20	12
The Effects of Changes in Foreign Exchange Rates	21	11
Borrowing Costs	23	16
Related Party Disclosures	24	18
Investment in Associates and Joint Ventures	28	23
Financial Reporting in Hyperinflationary Economies	29	-
Financial Instruments: Presentation	32	31
Earnings per Share	33	20
Interim Financial Reporting	34	25

Title of Ind AS	Ind AS	AS
Impairment of Assets	36	28
Provisions, Contingent Liabilities and Contingent Assets	37	29
Intangible Assets	38	26
Investment Property	40	13
Agriculture	41	-
First - time Adoption of Indian Accounting Standards	101	-
Share Based Payment	102	Guidance Note issued by ICAI and guidelines issued by Securities and Exchange Board of India (SEBI)
Business Combinations	103	14
Insurance Contracts	104	Circulars and notifications issued by IRDA
Non-current Assets Held for Sale and Discontinued Operations	105	24
Exploration for and Evaluation of Mineral Resources	106	Guidance Note 15
Financial Instruments: Disclosures	107	32
Operating Segments	108	17
Financial Instruments	109	30
Consolidated Financial Statements	110	21
Joint Arrangements	111	27
Disclosure of Interests in Other Entities	112	-
Fair Value Measurement	113	-
Regulatory Deferral Accounts	114	Guidance Note

7. This analysis is based on the requirements of Ind AS which are presently applicable to Indian companies, and does not cover the impact of any future amendments



Annexure 3

Areas of impact not affecting transfer pricing benchmarking analysis[8]

Nature of standard	Ind AS	Particulars
Disclosures	1	Presentation of financial statements
	7	Statement of cash flows
	10	Events after the Reporting Period
	24	Related Party Disclosures[9]
	33	Earnings per Share
	34	Interim Financial Reporting
	107	Financial Instruments: Disclosures
	108	Operating Segments
Recognition and Measurement	2	Inventories
	12	Income Taxes
	23	Borrowing Cost
	32	Financial Instruments: Presentation[10]
	36	Impairment of Assets
	40	Investment Property
	105	Non-current Assets Held for Sale and Discontinued Operations
Consolidated financial statements	28	Investments in associates
	103	Business Combinations
	110	Consolidated Financial Statements[11]
	111	Joint Arrangements
	112	Disclosure of Interests in Other Entities

8. This paper does not cover Ind AS 29 - Financial Reporting in Hyperinflationary Economies, Ind AS 41 - Agriculture, Ind AS 104 - Insurance contracts, Ind AS 106 - Exploration for evaluation of mineral resources, Ind AS 114 - Regulatory Deferral Accounts as these standards are specific to those industries.
9. Ind AS on related party disclosures may have an impact on the reporting in Form 3CEB.
10. This Ind AS would impact the recognition, measurement and presentation of preference shares/ perpetual debenture/Compulsorily convertible debentures.
11. Ind AS on consolidated financial statements may impact CbyC reporting.

Annexure 4

Snapshot of the areas that have an impact on transfer pricing benchmarking analysis

Ind AS	Particulars	Operating/ Non operating
8	Accounting Policies, Changes in Accounting Estimates and Errors	Operating
11	Construction Contracts[12]	Operating
16	Plant, Property and Equipment	Operating
17	Leases	Operating
18	Revenue	Operating
19	Employees Benefits	Operating
20	Government Grants	Operating
21	Effects of Foreign Exchanges	Operating
37	Provisions, Contingent Liabilities and Contingent Assets	Operating
38	Intangible Assets	Operating / Non operating[13]
101[14]	First-time Adoption of Indian Accounting Standards	Operating
102	Share based payments	Operating
109	Financial Instruments	Operating
113[15]	Fair Value Measurement	Operating

12. This Ind AS relates specifically to build, operate and transfer operations, hence we can look at making the adjustments on a case to case basis.
13. As discussed in Annexure 1, some changes in Intangibles assets have an impact on both operating and non-operating line items
14. This Ind AS has an impact on multiple accounting standards and hence has been discussed along with the relevant accounting standard.
15. Ibid

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