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IFRS Notes

Guidance note on Ind AS Schedule III – Key clarifications

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Introduction

The Schedule III to the Companies Act, 2013 (2013 Act) became applicable to all companies for the preparation of financial statements for financial years beginning on or from 1 April 2014. Schedule III provides general instructions for preparation of the balance sheet and the statement of profit and loss of a company.

The Ministry of Corporate Affairs (MCA) through a notification dated 16 February 2015 issued the Companies (Indian Accounting Standards) Rules, 2015 (Ind AS Rules) which laid down a road map for entities (other than insurance entities, banking entities and Non-Banking Financial Companies (NBFCs) (corporate road map) for implementation of Indian Accounting Standards (Ind AS) (converged with International Financial Reporting Standards (IFRS)) in a phased manner.

On 6 April 2016, MCA amended Schedule III to include general instructions for preparation of financial statements of a company whose financial statements are required to comply with Ind AS. The amendment divides Schedule III into two parts i.e. Division I and II:

- Division I is applicable to a company whose financial statements are required to comply with the current accounting standards
- Division II is applicable to a company whose financial statements are drawn up in compliance with Ind AS (Ind AS Schedule III).

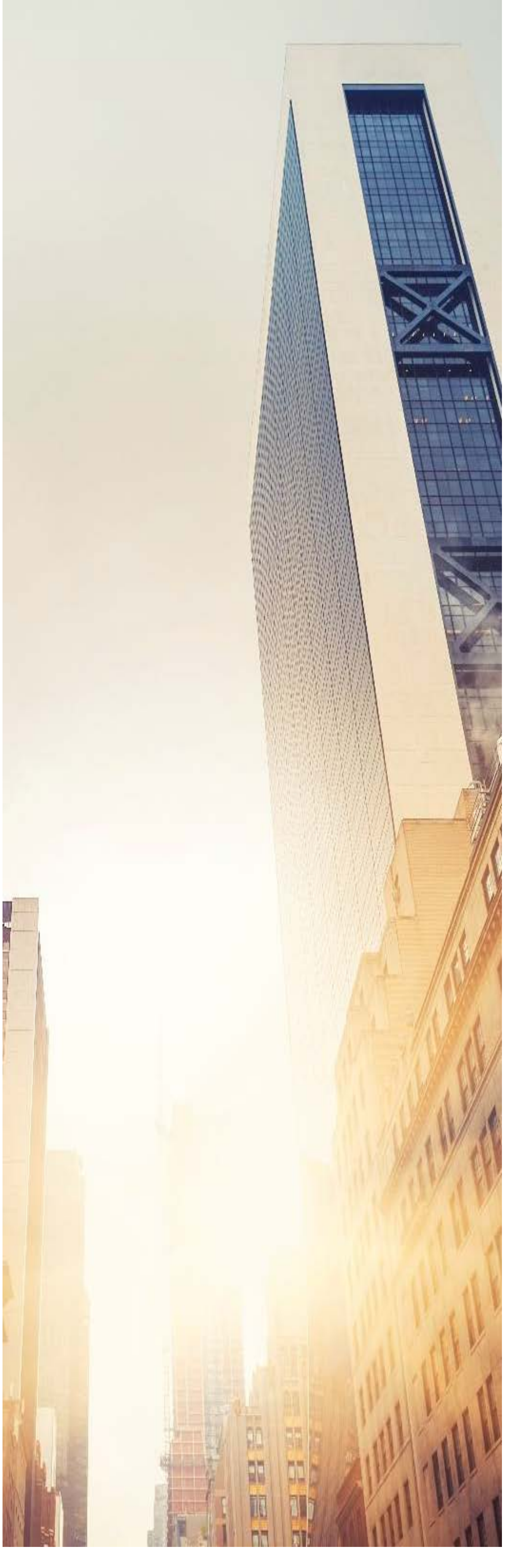
The Institute of Chartered Accountants of India (ICAI) on 20 April 2017 issued an exposure draft on the Guidance Note (GN) on Division II - Ind AS Schedule III to the 2013 Act which was open for comments until 30 April 2017.

New development

The ICAI on 27 July 2017 issued the GN on Division II - Ind AS Schedule III to the 2013 Act. The primary focus of the GN is to provide guidance in the preparation and presentation of financial statements in accordance with various aspects of Ind AS Schedule III, for entities adopting Ind AS. The GN has been structured in the following categories:

- Guidance on each of the line item of the balance sheet, statement of profit and loss
- Major differences in Division I and Division II of the Schedule III to the 2013 Act
- Illustrative format for stand-alone financial statement and consolidated financial statement
- Illustrations that provide guidance on application of the principles provided in the GN.

This issue of IFRS Notes provides an overview of some of the significant clarifications/guidance provided in the GN issued by the ICAI.



Overview of the GN

I. Main principles

The following are the main principles highlighted in the GN relating to preparation of financial statements in accordance with the Ind AS Schedule III:

- **2013 Act and Ind AS guidance vs Ind AS Schedule III requirements:** If compliance with the requirements of the 2013 Act, including Ind AS applicable to companies, requires any change in presentation or disclosure in the Ind AS financial statements, then Ind AS Schedule III would stand modified accordingly. This indicates that the requirements of the 2013 Act and Ind AS would prevail over the guidance in Ind AS Schedule III.
- **Liquidity presentation of balance sheet in the notes:** Companies may elect to present assets and liabilities in the order of liquidity as additional information in the Notes to the financial statements, since Ind AS Schedule III does not permit such presentation in the balance sheet.
- **Hierarchy of Ind AS guidance:** Terms used in Ind AS Schedule III are to be interpreted based on their meaning as defined in the relevant Ind AS or in the framework for preparation and presentation of financial statements in accordance with Ind AS (Ind AS framework) issued by ICAI. In the absence of such guidance, companies may consider the principles in paragraphs 10 to 12 of Ind AS 8, *Accounting policies, changes in accounting estimates and errors* (including referring to the most recent guidance issued by the International Accounting Standards Board) to develop and apply an accounting policy.

II. General instructions for preparation of balance sheet in the stand-alone financial statements

General instruction for preparation of balance sheet are provided in the Schedule III and relevant Ind AS standards. The following points highlight additional guidance provided in the GN:

a) Property, Plant and Equipment (PPE)

- *Previous Generally Accepted Accounting Principles (GAAP) information* (8.1.1.3): If the company has applied the deemed cost exemption at the date of transition to Ind AS, it may disclose information regarding the following under previous GAAP only as an additional information by way of a note forming part of the financial statements:
  - Gross block of assets
  - Accumulated depreciation
  - Provision for impairment.
- *Presentation of land and building* (8.1.1.6): Ind AS 16, *Property, Plant and Equipment* allows for grouping land and building under the same class for revaluation purposes, while in Ind AS Schedule III, land and buildings are presented as two separate classes of PPE. The GN states that companies should continue to present land and building separately as per Ind AS Schedule III and such presentation should be followed consistently.

b) Investments

- *Classification of investments (8.1.8.6):*
  - Ind AS Schedule III does not set out whether investments should be first disclosed as per category as per Ind AS 109, *Financial Instruments* (for example; measured at amortised cost, mandatorily measured at Fair Value Through Profit and Loss (FVTPL), designated at FVTPL, etc.) or by nature (for example; investment in equity instruments, investment in preference shares, etc.)
  - Ind AS Schedule III allows addition or substitution of line items on the face of the financial statements in order to comply with the 2013 Act or with Ind AS.
  - The GN clarifies that companies may disclose investments by grouping them in the following manner:
    - o Broad categories as per Ind AS 107, *Financial Instruments: Disclosures*
    - o Under each broad categorisation, nature-based classification as per Ind AS Schedule III
    - o Under each nature-based classification, grouping based on the relationship of bodies corporate (viz., subsidiaries, associates, joint ventures, and structured entities) as required by Ind AS Schedule III
    - o Under each grouping of bodies corporate, details giving names of and nature and extent of investments in bodies corporate as required by Ind AS Schedule III.

  Where a company chooses not to provide investment details in the format given above, it could present the information in other ways by changing the order of grouping. For example, investments may be classified first as per their nature and then within each nature – sub-classified into broad categories.

Overview of the GN (cont.)

- *Details regarding names of bodies corporate and nature and extent of the investment made* (8.1.8.1):
  - Ind AS Schedule III requires companies to give names of the bodies corporate that are subsidiaries, associates, joint ventures or structured entities. *It has done away with the requirement to give names of all body corporates in which the company has made any form of investment (i.e. equity shares, preference shares, debentures, etc.), except as mentioned below for investments designated at Fair Value Through Other Comprehensive Income (FVOCI)*. [This requirement is still present in AS Schedule III.]
  - Companies to disclose the names, number of equity instruments held and the face value of such instruments of all other bodies corporate for which they have designated the investments in equity instruments at FVOCI. This indicates that, in practice, companies may still be required to disclose this information for most investments in equity instruments.
  - Under each sub-classification of investments, disclose:
    - Names, nature and extent of the investment in each body corporate which is a subsidiary, associate, joint venture or structured entity; i.e. the number of such instruments held and face value of such instruments
    - Disclose separately whether investments are fully or partly paid.
- *Disclosure of aggregate amount of investments and market value thereof* (8.1.8.2):
  - Market value of quoted investments would generally mean disclosure of the 'fair value' of quoted investments as at each reporting date. However, based on the company's evaluation, if it determines that a quoted price does not represent fair value, then the company shall disclose the market value of quoted investments based on the quoted price which would be different from the investment's fair value.
  - Where the investments are measured at either FVTPL or FVOCI, as per Ind AS 109, the carrying amount and the market value of such investments are expected to be same and should be disclosed accordingly.
  - Quoted investments to mean an investment in respect of which there has been granted a quotation or permission to deal on a recognised stock exchange.
- *Aggregate amount for impairment in value of investments (*8.1.8.3):
  - GN requires that loss allowances for Expected Credit Losses (ECL) on financial assets measured at amortised cost are to be presented as an adjustment to the amortised cost of the investment.
  - For debt securities at FVOCI, a company is required to estimate a portion of fair value change, if any, attributable to a change in credit risk of such investment, by applying the impairment requirements of Ind AS 109 in recognising and measuring the loss allowance. The loss allowance is charged to profit or loss with a corresponding impact in Other Comprehensive Income (OCI). In other words, the company should not reduce the carrying amount of such investment in the balance sheet as the investment needs to be presented at fair value.
  - All equity instruments measured at Fair Value (FV) and all other investments measured at FVTPL do not require a separate calculation/evaluation of impairment amount. Hence in case of such investments, this disclosure is not applicable.
  - Disclosure of aggregate provision for impairment in the value of investments would be equal to the aggregate amount of impairment recognised and measured in accordance with Ind AS 109.
  - The aggregate provision for impairment in the value of investments may be either presented in totality for all its investments or separately for each class of investments (e.g., 'Investment in amortised cost', 'Investment in FVOCI') disclosed in the financial statements.
- *Investments in subsidiaries/associates/joint ventures* (8.1.8.4)
  - Ind AS 32, *Financial Instruments: Presentation* Ind AS 107 and Ind AS 109 scope out those interests in subsidiaries, associates, joint ventures that are accounted for in accordance with Ind AS 110, *Consolidated Financial Statements,* Ind AS 27, *Separate Financial Statements*

Overview of the GN (cont.)

or Ind AS 28, *Investments in Associates and Joint Ventures.* However, such investments still meet the definition of financial instruments and may be presented as a separate line item on the face of a company's stand-alone balance sheet. In any case, the disclosure requirements of Ind AS 107 would not apply to such investments.

- In some cases, Ind AS 110, Ind AS 27 or Ind AS 28 require or permit a company to account for an interest in a subsidiary, associate or joint venture in accordance with Ind AS 109. Accordingly, only in its stand-alone financial statements, the company shall present such interests in a subsidiary, associate or joint venture under the head 'Investments' separately on the face of a company's standalone balance sheet or in the notes, grouped under 'Financial Assets'. Such presentation would be in line with the guidance provided in para 8.1.8.6 and disclosure requirements of Ind AS 107 would also apply.
- For a company's Consolidated Financial Statements (CFS), investments accounted using the equity method (i.e. associates and joint ventures) should be shown as a separate line item, separately from financial assets as per the requirements of Ind AS 1, *Presentation of Financial Statements* para 54.

- *Investments in structured entities* (8.1.8.5)
  - Ind AS Schedule III requires disclosure of the nature and extent of the investments so made. As a structured entity is an entity that has been designed so that voting or similar rights are not the dominant factor in deciding who controls the entity, a brief description of the nature of contracts may be provided along with the rights held in such companies as evidenced by such contracts.

c) Non-current and current trade receivables and loans (8.1.9 – 8.1.10, 8.1.15)

- GN specifies that impairment loss allowance would not reduce the carrying amount of trade receivables. Companies should separately disclose the amount of loss allowance, presented in a separate line item as a deduction from the gross carrying amount of the trade receivables.
- In disclosing a trade receivable as 'doubtful', companies should disclose the amount of credit loss that is expected on that trade receivable. The balance amount of trade receivable other than the amount considered as doubtful should be disclosed as 'good'. Reference has been drawn from Ind AS 109 which defines 'credit loss' as 'the difference between all contractual cash flows that are due to a company in accordance with the contract and all the cash flows that the company expects to receive (i.e. cash shortfalls), including cash flows from the sale of collateral held.'
- Loans given should also be disclosed as 'doubtful' or 'good' on similar lines as followed for trade receivables above.
- Apart from the specific guidance included in the GN on current trade receivables, certain guidance given under non-current trade receivables that is relevant for current trade receivables, would also be applicable.

d) Other non-current assets (8.1.11)

- Ind AS Schedule III specifically requires bank deposits with more than 12 months maturity to be disclosed as a part of 'other financial assets' under financial, non-current assets. The GN mentions that the maturity should be construed as remaining maturity of more than 12 months.
- Ind AS Schedule III does not specify about the presentation of finance lease receivables unlike finance lease obligations which are to be grouped under 'Financial Liabilities'. The GN states that the non-current portion of a finance lease receivable should be presented under 'Other non-current financial assets' while its current portion should be presented under 'Other current financial assets'. The disclosure requirements of Ind AS 107 would apply to such receivables.

e) Cash and bank balances (8.1.16)

- The GN clarifies that the bank overdraft, in the balance sheet, should be included as 'borrowings' under financial liabilities.

f) Equity share capital

- *Instruments entirely equity in nature* (8.2.1.7): Instruments entirely equity in nature (for example; compulsorily convertible preference shares, compulsorily convertible debentures, etc.) may be presented as a separate line item on the face of the balance sheet under 'equity' after 'equity share capital' but before 'other equity'. Ind AS Schedule III permits the additional line items to be presented when such presentation is relevant to an

Overview of the GN (cont.)

understanding of the company's financial position or performance. The GN provides an illustration for presentation of reconciliation for instruments entirely equity in nature in the statement of changes in equity. Instruments that meet the definition of 'equity' under Ind AS 32 in their entirety and that do not have any component of liability shall be termed as 'Instruments entirely equity in nature'.

- *Equity component of a compound financial instrument (*8.2.1.10): Companies should provide all relevant disclosures for an equity component of a financial instrument that apply to 'equity share capital' (to the extent applicable). Since this item represents a component of an instrument, companies may need to provide extensive disclosures based on the terms of the entire compound instrument.
- *Terms of any security convertible into equity/preference shares* (8.2.1.20)*:* Disclosure is required for any instruments convertible into equity or preference shares. This disclosure is recommended for instruments that are entirely equity in nature and compound instruments that have an equity component and a liability component. It is clarified that in order to avoid duplication of disclosures, this disclosure is not required for instruments which are entirely liability in nature since similar disclosure needs to be provided as part of 'borrowings'. Companies may consider inserting a reference to the relevant disclosure provided under 'borrowings'.

g) Reserves and surplus (8.2.2.1)

- The GN provides specific guidance from the respective Ind AS on every line item to be presented under 'Reserves and Surplus'. Some of the key guidance provided under this head is as follows:
  - *Capital reserves:* Profit on re-issue of forfeited shares should be credited to capital reserve. Similarly, a gain on bargain purchase arising in a business combination where clear evidence of the underlying reasons does not exist, should be recognised directly in equity as capital reserve.
  - *Gain/loss on changes in the proportion held by Non-Controlling Interests (NCI)* (8.2.2.2): Ind AS 110, Ind AS 1 and Ind AS Schedule III do not specify where gain or loss on changes in the NCI should be presented i.e. whether they should be presented separately under 'capital reserve' or under 'other reserves'. In this regard, the GN mentions that a company may present such gain/loss separately as NCI reserve shown under 'other reserves' by specifying the nature.
  - *Re-measurement of net defined liability (8.2.2.3):* A company should present the accumulated re-measurements of defined benefit plans at the end of each reporting period as part of retained earnings.
  - *Securities premium account* (8.2.2.1)*:* Though the terminology used in Ind AS Schedule III is securities premium reserve, the GN clarifies to use the terminology as per the 2013 Act i.e. 'securities premium account'.
  - *Others:* The GN provides specific guidance from the respective Ind AS for other items of reserves and surplus, such as:
    - Debt instruments through OCI
    - Equity instruments through OCI
    - Effective portion of cash flow hedge reserve
    - Revaluation surplus
    - Exchange differences on translating the financial statements of a foreign operation,
    - Other items of OCI
    - Money received against share warrants, etc.

h) Other current financial liabilities (8.2.10)

- *Current maturities of long term debt:* Ind AS Schedule III requires presenting 'Current maturities of long-term debt' under 'Other financial liabilities' grouped under 'Current liabilities'. Long-term debt is specified in Ind AS Schedule III as a borrowing having a period of more than 12 months at the time of origination. While current maturities of long-term debt are in the nature of 'Borrowings', since Ind AS Schedule III specifically provides a separate line item for presenting current maturities of long-term debt under Other financial liabilities, it is recommended that companies follow the presentation requirements of Ind AS Schedule III.
- *Interest accrued:* Interest accrued on financial liabilities should form part of the financial liabilities' carrying amount whether they are at amortised cost (i.e. as per Effective Interest Rate method (EIR)), or at

Overview of the GN (cont.)

fair value. Accordingly, a company may not present 'Interest Accrued' separately from the related financial liability.

i) **Contingent liabilities and commitments** (8.2.14.2)

- Ind AS Schedule III does not require disclosure of financial guarantee as a contingent liability as a financial guarantee is recognised in the financial statements under Ind AS 109. The GN clarifies that entities are required to disclose guarantees other than financial guarantees as part of contingent liabilities.

j) **Specified Bank Notes (SBNs)** (8.5)

- The GN provides that companies may disclose separately, the details about SBNs as required, in the notes to accounts. It provides reference to the implementation guide on auditor's report issued by the ICAI for appropriate disclosures under this head.

III. General instructions for preparation of profit and loss in the stand-alone financial statements

General instruction for preparation of statement of profit and loss are provided in the Ind AS Schedule III and relevant Ind AS standards. Following points highlight additional guidance provided in the GN:

a) **Revenue from operations** (9.1.6): The collection of Goods and Services Tax (GST) by an entity would not be an inflow on the entity's own account but it shall be made on behalf of the government authorities. Accordingly, the GN clarifies that the revenue should be presented net of GST.

b) **Other income** (9.2): Interest income on financial assets measured at amortised cost and financial assets (debt instruments) at FVOCI, calculated using the EIR method, and should be presented in separate line items under 'Other income'.

Interest income on financial assets measured at FVTPL is included as part of fair value changes. Accordingly, a company should disclose as its accounting policy whether it presents interest income on financial assets at FVTPL as part of fair value changes or presents it separately. Additionally, the GN also prescribes the nature of line items and manner of disclosure for net fair value gains or losses on financial assets measured at FVTPL. It mentions that the according to Ind AS 107 fair value gains or losses (net) on financial assets at FVTPL should be presented under 'other non-operating income'.

For other non-operating income, income should be disclosed net off expenses directly attributable to such income. However, the expenses so netted off should be separately disclosed.

c) **Finance costs** (9.5.5)

- *Interest expense:* The GN specifies the following types of finance charges to be shown under this head:
  - Interest cost on financial liabilities measured at amortised cost (e.g., borrowings from banks and others, on debentures, bonds or similar instruments etc.) calculated as per the effective interest method
  - Unwinding of the discount that results in an increase in financial liabilities such as security deposits for assets taken on lease
  - Increases in the carrying amount of provisions/decommissioning liabilities where such increase reflects the passage of time
  - Finance charges on finance leases that are in the nature of interest expense
  - Net interest on net defined benefit liability which reflects the change in net defined benefit liability that arises from the passage of time.

  The GN specifies that all of the above should be classified as interest expenses except that a company has a choice in presenting the net interest on net defined benefit liability, which reflects the change in net defined benefit liability that arises from the passage of time, as employee benefit costs.

  Further, Ind AS 107 para 20(b) requires total interest expense calculated using the effective interest method for financial liabilities that are not measured at FVTPL to be shown separately. Accordingly, the GN mentions that the same should be presented as a separate line item under 'Finance costs'.

- *Dividend on redeemable preference shares:*
  - Dividend on preferences shares, whether redeemable or convertible, is of the nature of 'interest expense', only where there is no discretion of the issuer over the payment of such dividends. In such a case, the portion of dividend as determined by applying the effective interest method should be

Overview of the GN (cont.)

presented as 'interest expense' under 'Finance cost'. Accordingly, the corresponding Dividend Distribution Tax (DDT) on such portion of non-discretionary dividends should also be presented in the statement of profit and loss under 'interest expense'.

  – Discretionary payments of dividend on preference shares, whether redeemable or convertible should be presented in statement of changes in equity and resultant DDT should also be presented in statement of changes in equity.

- *Exchange differences regarded as an adjustment to borrowing costs:* Foreign exchange differences relating to foreign currency borrowings to the extent not capitalised under Ind AS 23, *Borrowing Costs* would be disclosed under finance costs.

  However, para 11.3 of the Ind AS Schedule III GN provides guidance on the net gain or loss on foreign currency translation (other than considered as finance cost) would be classified under other expenses and such amount should be separately disclosed.

d) Deferred tax (9.7.2)

- Minimum Alternative Tax (MAT) credit entitlement should be grouped with deferred tax asset (net) in the balance sheet and a separate note should be provided specifying the nature and amount of MAT credit included in the deferred tax. The company should review at each balance sheet date the reasonable certainty to recover deferred tax asset including MAT credit entitlement.

e) Profit/(loss) from discontinued operations (9.8)

- Profit or loss from discontinued operations needs to be separately disclosed on the face of the statement of profit and loss. If a single amount of profit or loss from discontinued operations is presented then additional disclosures analysing this single amount should be presented by a company either in the notes or on the face of the statement of profit and loss (as per requirements of Ind AS 105, *Non-current Assets Held for Sale and Discontinued Operations*) and the disclosure would include the following items:
  – The revenue, expenses and pre-tax profit or loss of discontinued operations
  – The gain or loss recognised on the measurement to fair value less costs to sell or on the disposal of the assets or disposal group(s) constituting the discontinued operation
  – The related income tax expense as required by paragraph 81(h) of Ind AS 12, *Income Taxes.*
- If the above analysis is presented in the statement of profit and loss, then it should be presented in a section identified as relating to discontinued operations i.e. separately from continuing operations.

f) OCI (10.3)

- The GN lists down additional components of OCI in line with Ind AS 1 (that are not included in the Ind AS Schedule III) such as:
  – Items that will not be reclassified to profit or loss and its related income tax effects:
    o Gains and losses on hedging instruments that hedge investments in equity instruments measured through OCI
  – Items that will be reclassified to profit or loss and its related income tax effects:
    o Changes in time value of options when separating the intrinsic value and time value of an option contract and designating only intrinsic value changes as the hedge instruments
    o Changes in the value of the forward elements of forward contracts when separating the forward element and spot element of a forward contract and designating only spot element changes as hedging instrument
    o Changes in the value of the foreign currency basis spread of a financial instrument when excluding it from the designation of that financial instrument as the hedging instrument.
- Guidance as per Ind AS 1 has been provided in the GN on presentation of tax effects of the items presented in OCI.
- In line with Ind AS 1 a company should present for each component of equity, an analysis of OCI either in the statement of changes in equity or in the notes to accounts.

Overview of the GN (cont.)

g) Additional information to be disclosed by notes to statement of profit and loss

- *Net gain or loss on sale of investments* (11.2)*:* A company should disclose the fair value gains or losses (net) on sale of financial assets which are measured at FVTPL (realised and unrealised both) as part of 'net gain on financial assets measured at FVTPL in the statement of profit and loss. However, the 'net gain or loss on sale of investments' should be presented separately by way of a note.
- *Changes in regulatory deferral account balances* (11.7): The GN includes guidance on Ind AS 114, *Regulatory Deferral Accounts* relating to items recognised in OCI and their related disclosures.

IV. General Instructions for preparation of CFS

- The requirements of Schedule III (as explained in the stand-alone financial statements' section) would be equally applicable in preparation of CFS and a company would provide disclosures relevant from the CFS perspective. Accordingly, following exemptions/modifications based on the relevance to the CFS:
  - *Share capital*: The GN mentions that it would be adequate to present paid up capital and any calls in arrears.
  - *Sources from which bonus shares are issued, e.g. capitalisation of profits or reserves or from securities premium account*: The GN mentions that this disclosure is not required as it is not relevant at the CFS level.
  - *Disclosures of all unutilised monies out of the issue indicating the form in which such unutilised funds have been invested:* The GN mentions that this disclosure is not required as it is not relevant at the CFS level.
  - *Materiality from CFS perspective*: A materiality threshold of 10 per cent of the respective balance sheet item should be considered while providing following disclosures:
    - Period and amount of continuing default as on the balance sheet date in repayment of borrowings and interest
    - Loans and advances due to directors or other officers of the company or any of them either severally or jointly with any other persons or amounts due by firms or private companies respectively in which any director is a partner or a director or a member should be separately stated
    - Debts due by directors or officers of the company or any of them either severally or jointly with any other person or debts due by firms or private companies respectively in which any director is a partner or a director or a member should be separately stated.
    - Where in respect of an issue of securities made for a specific purpose, the whole or part of the amount has not been used for the specific purpose at the balance sheet date, there shall be indicated by way of note how such unutilised amounts have been used or invested.
  - *Share application money pending allotment shall be classified into equity or liability in accordance with relevant Ind AS*: The GN mentions that separate disclosure should be given for such monies due outside the group in respect of entities which are consolidated.
  - *Additional disclosures*: The GN mentions that certain disclosures such as payments to auditors, amounts of expenditure incurred on corporate social responsibility, disclosures on Micro, Small and Medium Enterprises Development (MSMED) Act, 2006 have no relevance at CFS level and may be dispensed with.

Our comments

The GN is a comprehensive guide for companies that are required to follow Ind AS Schedule III in presenting their Ind AS financial statements. It brings together presentation and disclosure guidance from the 2013 Act and the relevant Ind AS.

The issuance of the GN is expected to provide further clarity to companies that are required to present their annual financial statements in accordance with the requirements of Ind AS Schedule III.

Our comments (Cont.)

Companies may consider the following aspects further when implementing the requirements of the GN:

- *Breach of loan covenant*: Ind AS 1, paragraph 74 permits a company to classify a long-term loan arrangement as 'non-current' even when the liability has become payable on demand on breach of a material provision, if the lender has agreed (prior to the date of approval of financial statements) to not demand payment as a consequence of the breach. The GN reiterates that Ind AS 1 covers only substantive breaches of long term loans and minor defaults of debt covenants would not result in the loan being classified as 'current' as long as the lender has not recalled the loan prior to the date of approval of financial statements.

  The GN provides an example of a breach relating to submission of quarterly financial information, which is considered as minor based on past experience and/or discussions with the lender. However, entities would need to evaluate whether a breach of a loan covenant is material in nature based on the specific facts and circumstances applicable at the time in order to determine whether the related long term loan should be classified as 'current' or 'non-current'.

- *Current and non-current classification*: The GN requires the presentation of investments as 'current' or 'non-current' based on whether the investments are intended to be sold within 12 months from the balance sheet date/realisable within the operating cycle. It also observes that the classification of financial assets as per Ind AS 109 would not determine their classification as 'current' or 'non-current', although it may be one of the factors that entities should consider.

  In this context, entities may further consider the following:

  – Derivatives that are classified as FVTPL, but are not held for trading purposes, may be classified as current and/or non-current based on their outstanding maturities.

  – Investments/financial assets that are not held for trading, but specifically designated as FVTPL, may be presented as non-current to the extent that they are not expected to be realised within 12 months of the reporting date/the entity's normal operating cycle.

- *Additional line items*: The GN states that as per Ind AS Schedule III, all items of assets and liabilities should be bifurcated between current and non-current portions. Where items presented under the 'non-current' head of the balance sheet do not have a corresponding 'current' head under the format given in Ind AS Schedule III, an additional line item may be used to classify the current portion of such items under the 'current' category. These guidelines indicate that additional line items may be used to present items for which no separate head is available in the Ind AS Schedule III format.

- *Interest income*: Paragraph 9.2 requires separate presentation in the statement of profit and loss of interest income calculated using the effective interest method. Ind AS 109 requires interest income on financial assets measured at amortised cost as well as debt instruments classified as FVOCI to be measured using EIR and presented as an interest income. The GN also permits companies to elect an accounting policy on whether interest income (computed based on EIR) on financial assets classified as FVTPL is presented separately from other fair value changes in the statement of profit and loss.

The following are some areas where companies may need further clarity from ICAI in order to implement and fully comply with the requirements of the GN:

- *Quoted investments*: Paragraph 8.1.8.2 requires disclosure of the aggregate amount of quoted investments along with their market value. The GN observes that while the term 'quoted' has not been defined in Ind AS Schedule III, 'quoted investment' means 'an investment in respect of which there has been granted a quotation or permission to deal on a recognised stock exchange'. Companies may have investments in securities that are traded in an active market and for which dealer or issuer quotes are available (for example, government securities or unlisted mutual funds). Further, clarity may be required from ICAI on whether investments in such instruments should be disclosed as 'quoted' or 'unquoted'. Conversely, there may be securities that are quoted on a recognised stock exchange but are not actively traded. For these investments quoted price may not represent fair value. The GN permits companies to disclose the aggregate amount of investments based on the quoted price in such a scenario, although the measurement of fair value for recognising such investments in the financial statements may differ from the quoted price.

- *ECL method*: Paragraph 8.1.8.3 of the GN requires a company to estimate a portion of the fair value change, if any, attributable to a change in credit risk of a debt investment classified as FVOCI, and disclose the same in the statement of profit and loss with a corresponding impact in OCI. We consider

Our comments (cont.)

that this amount (being the impairment allowance on the debt investments at FVOCI) should be estimated on the basis of the ECL model as required by Ind AS 109, i.e. based on the present value of expected cash shortfalls rather than the portion of the fair value change attributable to a change in credit risk.

- *Trade receivable*: Paragraph 8.1.9 states that in disclosing a trade receivable as 'doubtful' a company should disclose the amount of credit loss expected on that trade receivable and the balance amount of the receivable should be disclosed as 'good'. The GN illustrates the format in which companies should present this disclosure. Ind AS 109 requires companies to adopt the ECL model to estimate the impairment loss on trade receivables. In accordance with this guidance, companies may adopt a simplified approach to measure ECL based on a provision matrix that considers historical loss rates adjusted on the basis of current and expected future economic conditions. This model requires companies to assess and estimate expected losses not only on receivables that are 'doubtful' in nature at the reporting date but also on receivables that are currently 'good' but may include an element of future expected losses based on this analysis. This suggests that disclosing the amount of ECL as 'doubtful' trade receivables and the balance amount as 'good' may not be in accordance with the methodology prescribed in Ind AS 109. ICAI may consider providing further clarity on this aspect.

- *Dividend and dividend distribution tax*: Paragraph 9.5.5 (B) of the GN requires the presentation of *a portion* of non-discretionary dividends (determined by applying the effective interest method) on redeemable or convertible preference shares as a part of finance costs, since these are considered to be in the nature of interest expense. Further, DDT on such portion of non-discretionary dividend payments should also be presented under 'other expenses'.

  For example, a preference share that is convertible into a fixed number of shares of the issuer at a future date and requires non-discretionary dividend payments until the date of conversion would be classified as a compound instrument. In this scenario, the mandatory dividend stream would be measured at its fair value (generally at the present value of future dividend payments) and recognised as a financial liability with the remaining issue price being recognised as an equity component. Interest expense would be recognised on the liability component at the effective interest rate (effectively unwinding the discount on the dividend stream) and a payment of dividend would be attributed towards interest expense as well as repayment of the recognised liability component. Therefore, in this scenario, *a portion* of the non-discretionary dividend payment (being the unwinding of the discount on the dividend stream) would be recognised as an interest expense.

  Paragraph 9.5.5 (B) also states that a payment of dividend on redeemable or convertible preference shares that is discretionary in nature is in the nature of a distribution of profit and should be presented in the statement of changes in equity. The corresponding DDT should also be presented in a similar manner.

  However, Ind AS 32 does not provide guidance on the presentation of discretionary dividends in a situation where all of the consideration received on issuance of a preference share is classified as a financial liability, i.e. none, or no more than a trivial amount, is allocated to or recognised as equity. For example, a preference share redeemable at a premium, with a discretionary dividend component, may be almost entirely classified as a financial liability. In the absence of specific guidance in Ind AS 32, a company may have been permitted to elect an accounting policy on whether to present the payment of discretionary dividends on such instruments as an interest expense in profit or loss (since these are dividend payments on an instrument which is almost wholly recognised as a liability), or as a distribution of profits in equity (since discretionary dividends are in the nature of an equity feature). Further clarity may be required from ICAI on whether the GN requires companies to adopt an accounting policy to present all such discretionary dividends in equity.

- *Presentation of gains or losses on derivatives*: The GN requires disclosure of gains or losses on derivatives as a separate line item presented under 'other income' in the statement of profit and loss. While there is no specific guidance in Ind AS, internationally, gains and losses on derivatives relating to investing and financing activities (e.g., gains and losses on interest rate swaps, or gains and losses on foreign currency forward contracts that hedge foreign currency borrowings) are generally presented as part of finance income or finance costs, respectively. Similarly, if a company discloses the results of operating activities, then gains and losses on derivatives that are normally regarded as being of an operating nature are generally disclosed as part of operating activities. ICAI may consider providing further clarity on the disclosure requirements for gains and losses on such derivatives.

KPMG in India

Ahmedabad
Commerce House V, 9th Floor
902 & 903, Near Vodafone House
Corporate Road, Prahalad Nagar
Ahmedabad 380 051
Tel: +91 79 4040 2200
Fax: +91 79 4040 2244

Bengaluru
Maruthi Info-Tech Centre
11-12/1, Inner Ring Road
Koramangala,
Bengaluru 560 071
Tel: +91 80 3980 6000
Fax: +91 80 3980 6999

Chandigarh
SCO 22-23 (Ist Floor)
Sector 8C, Madhya Marg
Chandigarh 160 009
Tel: +91 172 393 5777/781
Fax: +91 172 393 5780

Chennai
No.10, Mahatma Gandhi Road
Nungambakkam
Chennai 600 034
Tel: +91 44 3914 5000
Fax: +91 44 3914 5999

Jaipur
Regus Radiant Centres Pvt. Ltd.
Level 6, Jaipur Centre Mall
B2 By Pass Tonk Road
Jaipur, Rajasthan 302 018
Tel: +91 141 710 3224

Gurgaon
Building No.10, 8th Floor
DLF Cyber City, Phase II
Gurgaon,
Haryana 122 002
Tel: +91 124 307 4000
Fax: +91 124 254 9101

Hyderabad
Reliance Humsafar, 4th Floor
8-2-618/2 Road No.11,
Banjara Hills
Hyderabad 500 034
Tel: +91 40 3046 5000
Fax: +91 40 3046 5299

Kochi
Syama Business Center
3rd Floor, NH By Pass Road,
Vytilla, Kochi – 682019
Tel: +91 484 302 7000
Fax: +91 484 302 7001

Kolkata
Unit No. 603 – 604, 6th Floor,
Tower - 1, Godrej Waterside,
Sector – V,
Salt Lake, Kolkata - 700 091
Tel: +91 33 44034000
Fax: +91 33 44034199

Mumbai
Lodha Excelus, Apollo Mills
N. M. Joshi Marg
Mahalaxmi, Mumbai 400 011
Tel: +91 22 3989 6000
Fax: +91 22 3983 6000

Noida
Unit No. 501, 5th Floor
Advant Navis Business Park
Tower B, Plot No. 07, Sector 142
Noida Expressway, Gautam Budh Nagar
Noida 201 305
Tel: +91 0120 386 8000
Fax: +91 0120 386 8999

Pune
9th Floor, Business Plaza
Westin Hotel Campus, 36/3-B
Koregaon Park Annex, Mundhwa Road
Ghorpadi, Pune 411 001
Tel: +91 20 6747 7000
Fax: +91 20 6747 7100

Vadodara
iPlex India Private Limited,
1st floor office space, No. 1004,
Vadodara Hyper, Dr. V S Marg
Alkapuri, Vadodara 390 007
Tel: +91 0265 235 1085/232 2607/
232 2672

You can reach out to us for feedback and questions at:
in-fmkpmgifrsinst@kpmg.com

KPMG in India's IFRS institute

Visit KPMG in India's IFRS institute - a web-based platform, which seeks to act as a wide-ranging site for information and updates on IFRS implementation in India.

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

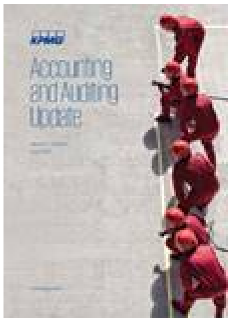
KPMG in India is pleased to present Voices on Reporting – a monthly series of knowledge sharing calls to discuss current and emerging issues relating to financial reporting.

Recently, the Central Board of Direct Taxes (CBDT) issued following circulars:

- Clarifications in the form of Frequently Asked Questions (FAQs) on issues relating to the levy of Minimum Alternate Tax (MAT) for Ind AS compliant companies
- Proposal for amendment to Section 115JB of the Income Tax Act, 1961 in relation to Ind AS compliant companies.

A special session of our Voices on Reporting webinar held on 3 August 2017 provided an overview of the implications of the above mentioned developments.

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



Issue no. 12/2017 – July 2017

This edition of Accounting and Auditing Update (AAU) analyses the impact of a Goods and Services Tax (GST) on Ind AS financial reporting.

As banks transition to Ind AS, they would need to compute effective interest on floating rate financial instruments under Ind AS 109, *Financial Instruments*. This a complex area of implementation and the standard does not prescribe an approach to compute Effective Interest Rate (EIR) in the case of floating rate financial instruments. In our article, we discuss alternative methods that banks may adopt for computing the EIR on floating-rate instruments held by them.

Our article emphasises the manner of selection and application of accounting policies along with disclosure requirements and how to present changes when there is a change in accounting policy.

Under the Companies Act, 2013 (2013 Act) section, we describe a provision relating to declaration and payment of dividend. The article also compares the requirements of the 2013 Act with the Securities and Exchange Board of India's (SEBI) regulations with regard to dividend.

Our publication also carries a regular synopsis of recent regulatory updates in India and internationally.

SEBI mandates disclosure of defaults on repayment of loans from banks by listed entities

16 August 2017

The SEBI (Listing Obligations and Disclosure Requirements) Regulations, 2015 require disclosure of material events/information by listed entities to stock exchanges. Specific disclosures on certain matters such as delays and default in payment of listed non-convertible debentures, listed non-convertible preference shares, foreign currency convertible bonds and other similar types of debt instruments.

The Listing Regulations do not require the above disclosures to be provided in respect of loans from banks and financial institutions.

The SEBI, through its circular dated 4 August 2017 has mandated listed entities who have defaulted in payment of interest/instalment obligations on loans from banks and financial institutions, debt securities (including commercial paper), etc. to provide a disclosure of defaults to the stock exchanges within one working day from the date of the default in the manner prescribed in the circular.

This circular is effective from 1 October 2017.

This First Notes provides an overview of the new SEBI disclosure requirements.

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