IFRS Notes

Ind AS Transition Facilitation Group (ITFG) issues Clarifications Bulletin 12

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Introduction

The Ind AS Transition Facilitation Group (ITFG) in its meeting considered certain issues received from the members of the Institute of Chartered Accountants of India (ICAI), and issued its Clarification Bulletin 12 on 23 October 2017 to provide clarifications on 11 application issues relating to Indian Accounting Standards (Ind AS).

Background

With Ind AS being applicable to corporates in a phased manner from 1 April 2016, the ICAI, on 11 January 2016 announced the formation of the ITFG in order to provide clarifications on issues arising due to applicability and/or implementation of Ind AS under the Companies (Indian Accounting Standards) Rules, 2015 (Ind AS Rules).

Since then, ITFG issued 11 bulletins to provide guidance on issues relating to the application of Ind AS.

This issue of IFRS Notes provides an overview of the clarifications issued by ITFG through its Bulletin 12.

Overview of the clarifications in ITFG's Bulletin 12

The following issues relating to the application of Ind AS have been clarified in this Bulletin:

- **Application of the revaluation model for Property, Plant and Equipment (PPE) (Issue 1):** The ITFG considered a situation where an entity covered under phase II of the Ind AS road map (i.e. Ind AS is applicable from 1 April 2017) has certain immovable properties such as land or building. The issue raised relates to whether such an entity is allowed to use the revaluation model under Ind AS 16, *Property, Plant and Equipment* to measure such immovable properties in its first Ind AS financial statements prepared for the period ending 31 March 2018.

  As per ITFG, an entity should first evaluate whether the land and building that it holds is an investment property based on the following definition in Ind AS 40, *Investment Property*:

  'An investment property is a property (land or a building, or part of a building, or both) held (by the owner or by the lessee under a finance lease) to earn rentals or for capital appreciation or both, rather than for:

  a) Use in the production or supply of goods or services or for administrative purposes or

  b) Sale in the ordinary course of business.'

  Ind AS 40 permits only the cost model to be applied for subsequent measurement of investment properties. Therefore, the revaluation model cannot be applied to such assets.

  However, if the land and buildings meet the following definition of PPE under Ind AS 16, the entity may elect to apply the cost model or the revaluation model for subsequent measurement:

  PPE are defined as *'tangible items that are:*

  a) Held for use in the production or supply of goods or services, for rental to others, or for administrative purposes and

  b) Expected to be used during more than one period.'

  Paragraph 29 of Ind AS 16 provides that an entity should choose either the cost model or the revaluation model as its accounting policy and apply that policy to an entire class of PPE.

  Based on the above, the ITFG clarified the following treatment in two scenarios:

  - **Land or building is classified as PPE**: Measure the land or building initially at cost. For subsequent measurement, the entity has an option to choose cost model or revaluation model.
  - **Land or building is classified as an investment property:** Only cost model could be used for initial and subsequent measurement.

  Another issue raised relates to whether the entity could opt for cost model for some class of PPE and apply revaluation model for other class of PPE in its first Ind AS financial statements prepared for the period ending 31 March 2018.

Overview of the clarifications in ITFG's Bulletin 12 (cont.)

The ITFG considered the guidance in paragraphs 36 and 37 of Ind AS 16 which state that 'if an item of PPE has been revalued, the entire class of PPE to which that asset belongs should be revalued.'

Based on the above, the ITFG clarified that the entity may elect to apply the revaluation model to a particular class of assets and cost model for another class of assets which are classified as PPE.

- **Adjustment to carrying amount of PPE on account of government grant received prior to transition (Issue 2):** As per paragraph D5 of Ind AS 101, *First-time Adoption of Ind AS*, an entity could elect to measure an item of PPE at the date of transition to Ind AS at its fair value and use that fair value as its deemed cost at that date.

  The ITFG considered a situation where an entity adopting Ind AS from FY2016-17 had received a government grant to purchase a fixed asset from the Central Government (CG) during the FY2012-13. The grant received was deducted from the carrying amount of the fixed asset in accordance with the previous Generally Accepted Accounting Principles (GAAP).

  The entity chose to measure the item of PPE at its fair value and use that as its deemed cost on the date of transition to Ind AS in accordance with paragraph D5 of Ind AS 101. However, as per Ind AS 20, *Accounting for Government Grants and Disclosure of Government Assistance* such a grant is required to be accounted as deferred income on the date of transition and deduction of the grant in arriving at the carrying amount of the asset is not permitted.

  The ITFG considered whether the entity would be required to adjust the carrying amount of fixed assets as per previous GAAP to reflect accounting treatment of the government grant as per Ind AS 20.

  The ITFG considered the guidance provided in paragraph 24 of Ind AS 113, *Fair Value Measurement* with respect to definition of fair value and clarified that the fair value of the asset that would be derived as per Ind AS 113 is the exit price that would be received to sell an asset in an orderly transaction. This is a market-based measurement, not an entity-specific measurement.

  Accordingly, it clarified that the fair value of the asset is independent of the government grant received on the asset and no adjustment with regard to the government grant should be made to the fair value of the PPE taken as deemed cost on the date of transition to Ind AS.

  However, the company is required to recognise the asset-related government grant outstanding on the transition date as deferred income in accordance with the requirements of Ind AS 20. The resultant adjustment should be made in retained earnings or, if appropriate, another category of equity at the date of transition to Ind AS.

- **Accounting treatment of financial guarantees**: Ind AS 109, *Financial Instruments* defines a financial guarantee contract as a contract that requires the issuer to make specified payments to reimburse the holder for a loss it incurs because a specified debtor fails to make payment when due in accordance with the original or modified terms of a debt instrument.

  Further paragraph B2.5 of Ind AS 109, *inter alia*, provides that financial guarantee contracts may have various legal forms, such as a guarantee, some types of letter of credit, a credit default contract or an insurance contract. However, their accounting treatment does not depend on their legal form.

  The ITFG opined on the following two issues with respect to the determination and accounting treatment of financial guarantee contracts:

  a) **Assessment of whether a comfort letter is a financial guarantee contract (Issue 3):** The ITFG considered a situation where a parent company has issued a comfort letter to its subsidiary company. The subsidiary company was able to obtain funds from its banker on the basis of such comfort letter. The issue considered is whether the comfort letter could be accounted for as a financial guarantee contract as per Ind AS 109 by the parent company.

     Based on the guidance provided in Ind AS 109, the ITFG clarified that a significant feature of a financial guarantee contract is the contractual obligation to make specified payment in case of default by the credit holder. The contract may not necessarily be called a financial guarantee contract and it may take any name or legal form. However the treatment would be same as that of a financial guarantee contract if a contract legally meets these requirements and falls within the definition in Ind AS 109.

     Therefore, in the given case, the parent company would be required to evaluate whether it is contractually obliged to make good the loss in case the subsidiary company

Overview of the clarifications in ITFG's Bulletin 12 (cont.)

fails to make the payment. If yes, then such comfort letter would be considered to be a financial guarantee contract and would be accounted for in accordance with Ind AS 109.

b) **Accounting treatment of financial guarantee for a loan taken by an associate company (Issue 11):** The ITFG considered a situation where a company (V Ltd.) adopting Ind AS from FY2017-18 has given a financial guarantee for five years against the loan taken by its associate company (S Ltd.) since 1 April 2014. V Ltd. charges 1 per cent guarantee commission from S Ltd.

The ITFG considered the value at which the financial guarantee contract would be accounted in the opening Ind AS balance sheet of V Ltd.

It clarified that if the financial guarantee meets the definition of a financial guarantee contract as per Ind AS 109 and the associate company (S Ltd.) pays the parent company (V Ltd.) a guarantee commission, then V Ltd. is required to determine if this commission represents the fair value of the financial guarantee contract. If the premium is equivalent to an amount that S Ltd. would have paid to obtain a similar guarantee in a standalone arm's length transaction, then at initial recognition the fair value of the financial guarantee contract is likely to equal the commission received.

The ITFG also considered the situation wherein the guarantee was invoked as on 31 March 2016 but V Ltd. continued to show it as a contingent liability in its previous GAAP financial statements of 2015 and also 2016 on the basis that the liability would not devolve on it. The issue considered is whether on the Ind AS transition date i.e. 1 April 2016, the impairment and fair value of the financial guarantee need to be calculated.

Paragraph 4.2.1 of Ind AS 109 requires that an entity should classify all financial liabilities as subsequently measured at amortised cost, except for financial guarantee contracts. Financial guarantee contracts should be subsequently measured at the higher of the following:

a) Amount of the loss allowance determined in accordance with Section 5.5 of Ind AS 109

b) Amount initially recognised less, when appropriate, the cumulative amount of income recognised in accordance with the principles of Ind AS 18, *Revenue.*

Based on the above, the ITFG clarified that the parent company (V Ltd.) should recognise a liability for the amount of premium received and subsequently measure the financial guarantee contract at the higher of the amount of loss allowance determined in accordance with Ind AS 109 and the amount initially recognised less cumulative amount of income recognised in accordance with Ind AS 18. Further, V Ltd. should estimate and recognise the expected loss in accordance with Ind AS 109 at the end of each reporting period.

- **Accounting for loan and processing fees paid in a refinancing arrangement (Issue 4):** The ITFG considered a situation where a company (PQR Ltd.) adopting Ind AS from FY2017-18 had obtained a loan from bank A in FY2013-14 and paid loan processing fees and commitment charges. PQR Ltd. availed a fresh loan from bank B in May 2017 as a take-over of facility i.e. the new loan was sanctioned to pay off the old loan taken from bank A. The company paid prepayment premium to bank A to clear the old term loan and paid processing fees to bank B for the new term loan.

  The issue considered was whether the prepayment premium as well as the processing fees would be treated as transaction costs of obtaining the new loan (as per Ind AS 109), in the financial statements of PQR Ltd. prepared in accordance with Ind AS for FY2017-18.

  Under Ind AS guidance, the loan processing fees solely relate to the origination of the new loan (i.e. do not represent loan modification/ renegotiation fees) and are in the nature of transaction costs, i.e. incremental costs that are directly attributable to the acquisition, issue or disposal of a financial asset or financial liability. Paragraph B5.4.2 of Ind AS 109, *inter alia*, provides that fees that are an integral part of the effective interest rate of a financial instrument include origination fees paid on issuing financial liabilities measured at amortised cost. These fees are an integral part of generating an involvement with a financial liability.

  Paragraph B5.4.8 of Ind AS 109 provides that the transaction costs include fees and commission paid to agents (including employees acting as selling agents), advisers, brokers and dealers, levies by regulatory agencies and security exchanges, and transfer taxes and duties. Transaction costs do not include debt premiums or discounts, financing costs or internal administrative or holding costs.

  Based on the above guidance, ITFG clarified that processing fees paid to avail a fresh loan from

Overview of the clarifications in ITFG's Bulletin 12 (cont.)

bank B would be considered as transaction cost in the nature of origination fees for the new loan and would be included while calculating effective interest rate as per Ind AS 109.

Since the original loan was prepaid, the prepayment would result in its extinguishment. According to paragraph 3.3.3 of Ind AS 109, the difference between the carrying amount of the financial liability extinguished and the consideration paid should be recognised in the statement of profit and loss. Further, where modification of terms is accounted for as an extinguishment, any costs or fees incurred are recognised as part of the gain or loss on the extinguishment.

Accordingly in the given case, the prepayment premium should be recognised as part of the gain or loss on extinguishment of the old loan. Further, the unamortised processing fee related to the old loan would also be required to be charged to the statement of profit and loss.

- **Treatment of intra-group profit in the Consolidated Financial Statements (CFS) (Issue 5):** The ITFG considered a situation where an associate company (ABC Ltd.) has been accounted under equity method in the CFS of company XYZ Ltd. under previous GAAP. However, due to the principles of defacto control as given under Ind AS 110, *Consolidated Financial Statements*, ABC Ltd. became a subsidiary of XYZ Ltd. under Ind AS. Before transition to Ind AS, company XYZ Ltd. sold some goods to ABC Ltd. at a profit margin of 10 per cent which is being used by ABC Ltd. for its operation i.e. these goods represent PPE. XYZ Ltd. opted to continue with the carrying value of PPE as per previous GAAP as its deemed cost. This situation required ITFG to consider whether the values appearing in the subsidiary's financial statements (i.e. ABC Ltd.) should be considered as deemed cost without any adjustment.

  The issue considered relates to whether such unrealised profits existing in the PPE require elimination at the consolidated level.

  The ITFG considered the guidance given under paragraph D7AA of Ind AS 101 which provides that a first-time adopter to Ind AS may elect to continue with the carrying value for all of its PPE as per previous GAAP and use that as its deemed cost as at the date of transition after making necessary adjustments permitted under Ind AS. It further provides that in the CFS, the previous GAAP amount of the subsidiary should be that amount used in preparing and presenting CFS. No further adjustments to the deemed cost of the PPE so determined in the opening balance sheet should be made for transition adjustments that might arise from the application of other Ind AS.

  However, Ind AS 110 requires full elimination of intra-group assets and liabilities, equity, income, expenses and cash flows relating to transactions between entities of the group (profits or losses resulting from intra group transactions that are recognised in assets such as inventory and fixed assets are eliminated in full).

  Therefore, based on the above, ITFG clarified that XYZ Ltd. would need to firstly eliminate the intra-group profit of 10 per cent recognised in the separate financial statements of ABC Ltd. and then should apply the deemed cost exemption under paragraph D7AA of Ind AS 101.

- **Applicability of Ind AS to an Indian branch office of a foreign company (Issue 6):** Rule 6 of the Ind AS Rules requires that an Indian company which is a subsidiary, associate, joint venture and other similar entities of a foreign company should prepare its financial statements in accordance with the Ind AS subject to meeting the criteria specified in the corporate road map.

  The ITFG clarified that a branch office of a foreign company established in India is not a company incorporated under the provisions of the Companies Act, 2013 (2013 Act). It is only an establishment/extension of a foreign company in India. Therefore, a branch office of a foreign company is not covered under Rule 6 of the Ind AS Rules and is not required to comply with Ind AS.

- **Accounting treatment of government loans at a below-market rate of interest (Issue 7):** Paragraph B10 of Ind AS 101 requires that a first-time adopter should apply the requirements in Ind AS 109 and Ind AS 20 prospectively to government loans existing at the date of transition to Ind AS. Therefore, the carrying amount of the government loan (under previous GAAP) would continue to be recognised at the date of transition to Ind AS. The benefit of obtaining the loan at a below-market interest rate (based on a retrospective restatement of the loan amount at its fair value on initial recognition) would not be recognised as a government grant since Ind AS 101 does not permit such retrospective restatement.

  Further, Ind AS 20 requires that the benefit of a government loan at a below-market rate of interest is treated as a government grant and should be accounted for in accordance with Ind AS 20.

Overview of the clarifications in ITFG's Bulletin 12 (cont.)

The ITFG considered a situation where a company has obtained a below-market rate of interest loan from government for five years, prior to transition to Ind AS. Under previous GAAP, the carrying amount of the loan was INR10,00,000 at the date of transition to Ind AS. The amount repayable would be INR10,05,000 at 1 April 2019 (end date of loan).

The issue considered by ITFG is whether the exemption under paragraph B10 would be available for the date of transition to Ind AS or all the subsequent period until the existing loan is presented i.e. up to 31 March 2019.

Based on the guidance given in Ind AS 101 and Ind AS 20, the ITFG clarified that a first-time adopter should use its previous GAAP carrying amount of the government loan as the Ind AS carrying amount on the date of transition. It should apply the requirements of Ind AS 20 and Ind AS 109 prospectively to government loans existing at the date of transition to Ind AS, unless the necessary information needed to apply the requirements of Ind AS 109 and Ind AS 20, retrospectively has been obtained at the time of initially accounting for that loan.

Since the company has not applied Ind AS 20 and Ind AS 109 retrospectively to government loans at the date of transition, the corresponding benefit of the government loan being at a below-market rate of interest should not be recognised as a government grant. Therefore, the effective interest rate of the loan should be computed by comparing the carrying amount of the loan at the date of transition with the amount and timing of expected repayment to the government.

Another related issue considered was whether the exemption given under paragraph B10 of Ind AS 101 would apply to deferment of a liability payable to government based on agreement i.e. liability similar to sales tax deferment for 10 years.

The ITFG clarified that in a scheme of deferral of sales tax, the amount of sales tax collected by the company from its customers is retained by the company and is required to be repaid after specified years (10 years in the above mentioned case). This makes such an arrangement similar in nature to an interest-free loan and hence the treatment as mentioned above should also be applied to such balances (of deferred sales tax liabilities) outstanding at the date of transition.

Therefore, in the above case, the company would recognise the government loan at INR10,00,000 at the transition date on applying the exemption. However, for subsequent measurement, it should calculate the effective interest rate on 1 April 2016 (i.e. the transition date).

- **Business combinations**: The ITFG has provided clarification on the following issues relating to business combinations in the Bulletin:

  a) **Determination of acquisition date in a scheme approved by National Company Law Tribunal (NCLT) (Issue 8)**: As per the provisions of Ind AS 103, *Business Combinations* an acquirer is required to identify the acquisition date which is the date on which it obtains control of the acquiree. Such a date is generally the closing date on which the acquirer legally transfers the consideration, acquires the assets and assumes the liabilities of the acquiree. However, an acquirer could obtain control on a date earlier or later than the closing date (e.g. a written agreement provides that the acquirer obtains control of the acquire on a date before closing date). An acquirer should consider all relevant facts and circumstances in making this assessment.

  As per the provisions of the 2013 Act (proviso to Section 232(3)), no scheme of arrangement would be sanctioned by the NCLT unless a certificate by the company's auditor has been filed with the NCLT to the effect that the accounting treatment, if any, proposed in the scheme of compromise or arrangement is in conformity with the accounting standards prescribed under Section 133 of the 2013 Act.

  The ITFG considered a situation where pursuant to a court scheme, a company is merged with another company with an appointed date approved by NCLT (as 1 April 2016) and the companies would prepare their first Ind AS financial statements for the year ending 31 March 2018. The issue relates to its accounting treatment and whether the merger (with appointed date prior to Ind AS implementation date) would have an impact on the certificate issued by the auditors on compliance of the scheme with Ind AS 103.

  The ITFG considered the guidance given in Ind AS 103 and opined that an entity is first required to assess whether the business combination is under common control or not.

Overview of the clarifications in ITFG's Bulletin 12 (cont.)

Accordingly, the following clarifications have been provided by ITFG:

i. **Business combination is under common control**: In such a case, an entity is required to restate its financial statements as if the business combination had occurred from the beginning of the preceding period in the financial statements.

   If an auditor considers that as per the proposed accounting treatment, the date from which the amalgamation is effected in the books of accounts of the amalgamated company is different from the acquisition date as per Ind AS 103 i.e. the date on which control has been actually transferred, then the auditor should state the same in the certificate to be issued under Section 232(3) of the 2013 Act.

   Additionally, if the NCLT approves the scheme with a different appointed date as compared to the acquisition date as per Ind AS 103, then the appointed date approved by the NCLT would be considered as the acquisition date for business combinations. The company would be required to provide appropriate disclosures and the auditor would need to consider the requirements of relevant auditing standards when issuing its certificate.

ii. **Business combination is not under common control**: In such a case, the date of acquisition is the date from which an acquirer obtains control of the acquiree.

   If an auditor considers that as per the proposed accounting treatment, the date from which the amalgamation is effected in the books of accounts of the amalgamated company is different from the acquisition date as per Ind AS 103 i.e. the date on which control has been actually transferred, then the auditor should state the same in the certificate to be issued under Section 232(3) of the 2013 Act.

   However, if the NCLT approves the scheme with a different appointed date as compared to the acquisition date as per Ind AS 103, then the appointed date approved by the NCLT would be considered as the acquisition date for the business combination. The company would be required to provide appropriate disclosures and the auditor would need to consider the requirements of relevant auditing standards.

b) **Retrospective application of Ind AS 109 to financial instruments acquired in past business combinations (Issue 9):** The ITFG considered a situation where a company (company A) covered under phase II of the Ind AS road map acquires another company (company B) in a scheme of amalgamation approved under the provisions of the 2013 Act with effect from 1 April 2015. Company A has elected to apply the option available under paragraph C1 of Ind AS 101 i.e. not to apply Ind AS 103 retrospectively to business combinations that occurred before the date of transition to Ind AS.

   The issue considered is whether company A would be required to apply Ind AS 109 retrospectively (i.e. from the date of origination of the financial instrument by company B) to financial instruments acquired as part of the business combination.

   The ITFG considered principles of paragraph C1 and C4 of Ind AS 101 which provide an option to companies to not restate past business combinations. If previous business combinations are not restated, the previous acquisition accounting remains unchanged.

   On the other hand, while preparing the opening Ind AS balance sheet, an entity is required to apply the criteria in Ind AS 109 to classify financial instruments on the basis of the facts and circumstances that exist at the date of transition to Ind AS. The resulting classifications are applied retrospectively.

   However, on application of the optional exemption in Ind AS 101 if the entity acquires the financial instruments in a past business combination, then their carrying amount in accordance with previous GAAP (as recognised immediately following the business combination) would be their deemed cost in accordance with Ind AS at that date.

   Based on the above guidance it has been further clarified that the requirements of Ind AS 109 need to be applied retrospectively, unless there is a transitional relief under Ind AS 101. While Ind AS 101 does not specifically provide any transitional relief for financial instruments, it does provide guidance on the accounting treatment if an entity elects not to restate past business combinations.

   Accordingly, in the present case, the carrying amount of the financial instruments acquired as part of the business combination under previous GAAP would be their deemed cost at the date of business combination.

Overview of the clarifications in ITFG's Bulletin 12 (cont.)

For such financial instruments, the fair value or amortised cost (as required by Ind AS 109) should be determined from the date of business combination and not from the date of origination of such financial instrument by the acquiree company. The financial instruments would be measured in the following manner:

i. **If financial instruments are classified as Fair Value Through Profit or Loss (FVTPL)/Fair Value Through Other Comprehensive Income (FVOCI):** Measure them at fair value at the date of transition to Ind AS

ii. **If financial instruments are classified at amortised cost:** Determine the carrying amount on the transition date based on the carrying amount of the loan at the date of business combination under previous GAAP, by applying the effective interest rate determined after considering the amount and timing of expected settlement of such financial instrument.

- **Adjustments to deemed cost, being the previous GAAP carrying amount of assets and liabilities (Issue 10):** Paragraph 10 of Ind AS 101 requires that an entity should in its opening Ind AS balance sheet apply the following steps:

  a) Recognise all assets and liabilities whose recognition is required by Ind AS

  b) Not recognise items as assets or liabilities if Ind AS do not permit such recognition

  c) Reclassify items that it recognised in accordance with previous GAAP as one type of asset, liability or component of equity, but are a different type of asset, liability or component of equity in accordance with Ind AS

  d) Apply Ind AS in measuring all recognised assets and liabilities.

  Based on the above, ITFG clarified that subject to any specific exemption/exception in Ind AS 101, all assets and liabilities are required to be recognised in accordance with the principles of Ind AS 101.

  The ITFG highlighted that there may be situations where no exemption /exception has been provided in respect of an item of asset and/or liability. However, application of Ind AS principles to such an item (to which no exemption/exception applies) has a corresponding impact on another item of asset and/or liability which is measured at its previous GAAP carrying amount at the transition date as permitted by Ind AS 101.

In such a situation, the adjustment to assets/ liabilities measured at deemed cost is only consequential in nature and arises due to the application of the transition requirements of Ind AS 101. Therefore, ITFG clarified that the previous GAAP carrying amount would need to be adjusted only to the extent of consequential adjustments. Except consequential adjustments, no further adjustment should be made due to application of other Ind AS, if an entity measure its assets/liabilities at deemed cost in accordance with previous GAAP carrying value as permitted under Ind AS 101 on the date of transition.

Previously, ITFG in its Bulletin 5 (issue 4 and issue 5) and Bulletin 10 (issue 1) considered and opined on certain specific consequential adjustments to the deemed cost of PPE/investments. Those issues have been summarised below:

a) **Accounting of processing fees by a company availing deemed cost exemption of PPE (Bulletin 5 - Issue 4):** A company capitalised processing fees on a loan taken before transition to Ind AS, as part of the cost of relevant fixed assets. It then availed the deemed cost exemption in Ind AS 101 to continue with the carrying amount of PPE as per previous GAAP. However, the loan was required to be measured at amortised cost as per Ind AS 109.

   The ITFG clarified that in the absence of any other mandatory exception or voluntary exemption applicable in this case, the carrying amount of loan is required to be restated to its amortised cost in accordance with Ind AS 109 as at the date of the transition. As a consequence, to restate the carrying amount of loan the carrying amount of fixed assets as at the date of the transition should also be reduced by the amount of processing cost (net of cumulative depreciation impact). This would be in the nature of consequential adjustment to enable an adjustment to the carrying amount of the loan as required by Ind AS.

b) **Accounting for government grant by a company availing deemed cost exemption of PPE (Bulletin 5 - Issue 5):** A company has received an asset related government grant prior to the date of transition to Ind AS and had deducted the grant received from the carrying amount of fixed assets, as permitted under previous GAAP. The company availed of the deemed cost exemption to continue with the carrying amount of PPE as per the previous GAAP.

Overview of the clarifications in ITFG's Bulletin 12 (cont.)

The company is required to recognise the asset related government grants outstanding on the transition date as deferred income in accordance with the requirements of Ind AS 20. As a consequence, to recognise the amount of unamortised deferred income as at the date of the transition in accordance with Ind AS 101, a consequential adjustment should be made to the carrying amount of PPE (net of cumulative depreciation impact) and retained earnings, respectively.

c) **Accounting for interest-free loan to subsidiary by a parent company availing deemed cost exemption for measuring its investment in subsidiary (Bulletin 10 - Issue 1)**: A parent company that has granted an interest-free loan to its subsidiary, has elected to measure its investment in the subsidiary at its previous GAAP carrying amount, being deemed cost in its separate financial statements, in accordance with paragraph D15 of Ind AS 101.

In this case, the differential in the carrying amount of the loan as per previous GAAP and its present value is in the nature of a consequential adjustment (due to application of Ind AS 109 to the loan) and should be added to the investment in subsidiary measured at cost.

Our comments

The ITFG clarifications are expected to resolve various practical implementation issues faced by companies that report their financial result under Ind AS or are transitioning to Ind AS. Companies should consider these interpretations when preparing their financial information. However, it should be noted that some of the issues require the exercise of judgement based on a consideration of facts and circumstances while analysing each individual situation.

Specifically, companies may consider the following aspects:

- **Accounting treatment of government loans at below-market rate of interest**: An important clarification relates to the accounting treatment for government loans at a below-market rate of interest that are outstanding on the date of transition to Ind AS. As per Ind AS 101, the requirements of Ind AS 109 and Ind AS 20 are to be applied prospectively to government loans existing at the transition date. Consequently, ITFG clarified that a first time adopter should use its previous GAAP carrying amount of the government loan as the Ind AS carrying amount on the date of transition.

  The corresponding benefit of the government loan being obtained at a below-market rate of interest would not be recognised as a government grant. This clarification would apply to interest-free deferrals of tax liabilities such as a sales tax deferral scheme availed by a company prior to transition. In this situation, the company would not be required to remeasure the deferred sales tax liability outstanding at the transition date.

- **Determination of acquisition date in case of a business combination that is not under common control**: In case of merger or amalgamation of entities pursuant to a court scheme where the appointed date approved by the NCLT was different to the acquisition date under Ind AS 103, ITFG clarified that the appointed date approved by the NCLT would be considered as the acquisition date for business combinations.

  This clarification is likely to have a significant impact since the approved appointed date could differ from the acquisition date as determined under Ind AS 103. Therefore, the accounting treatment based on the appointed date being considered as the acquisition date may not be in accordance with the standards prescribed under the 2013 Act. Companies should consider the impact of this clarification on their schemes and determine the appropriate disclosure to be made in their financial statements if the appointed date approved by the NCLT is different from the acquisition date under Ind AS 103. Further, ITFG requires auditors to consider the requirements of relevant auditing standards in their certificates to be issued under the 2013 Act.

- **Consequential adjustments to deemed cost, being previous GAAP carrying amount of PPE**: In its previous bulletins, the ITFG had opined on specific adjustments that would have a consequential impact on the deemed cost of PPE (being the previous GAAP carrying amount), such as government grants or loan origination costs previously adjusted in the carrying amount of PPE.

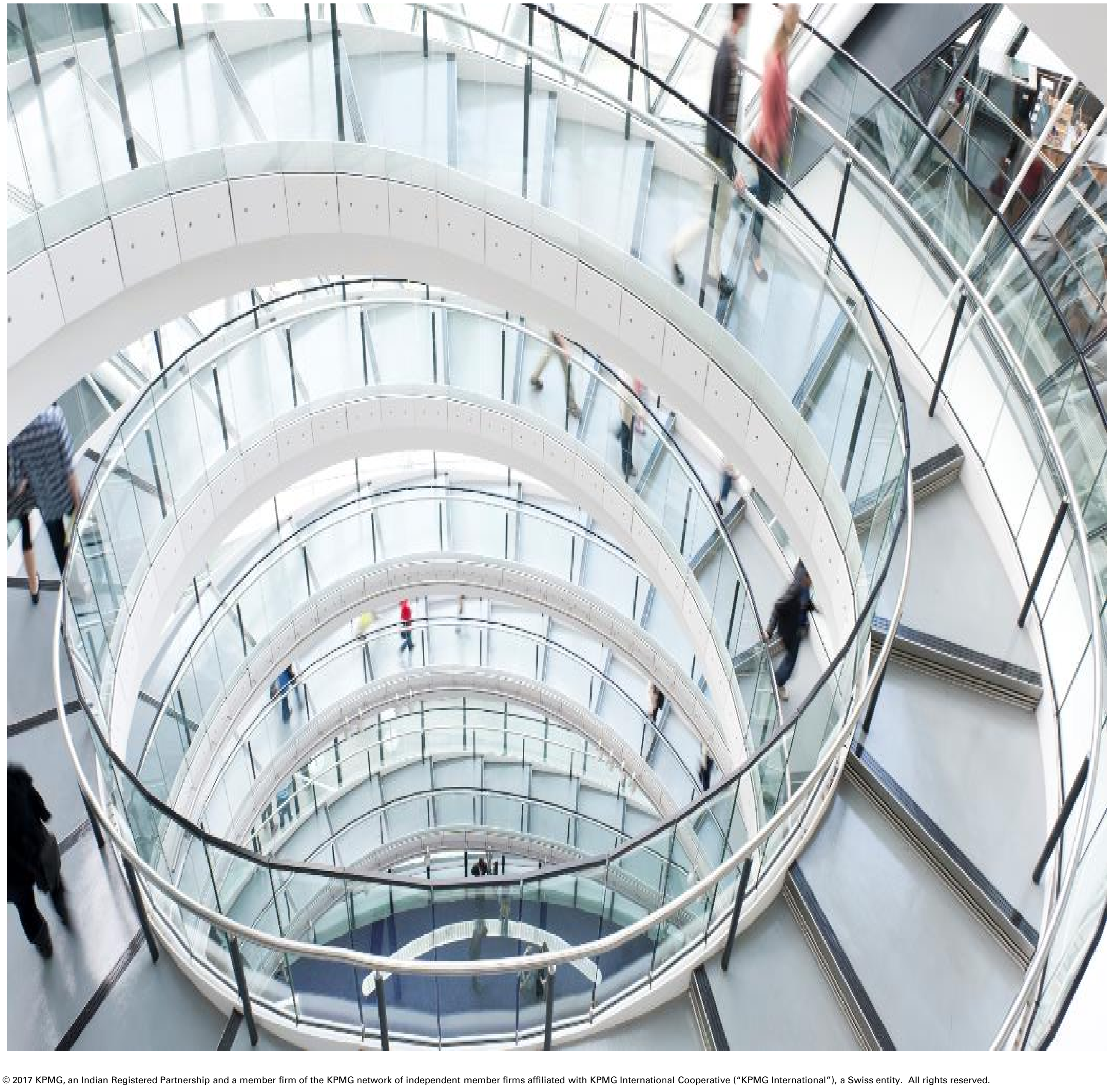
  In this bulletin, the ITFG has provided a clarification that is more general in nature and states that any adjustment to the previous GAAP carrying amount of PPE that is consequential in nature and arising as

Our comments (cont.)

a result of retrospective application of other Ind AS would be permitted. However, where companies have determined the deemed cost of PPE based on its fair value at the date of transition, Ind AS 109 does not permit any further adjustments to the deemed cost. Therefore, deemed cost (being fair value on transition) would not be adjusted as a result of application of other Ind AS and any consequential adjustments would have to be recognised in the retained earnings.

This clarification may result in additional adjustments being made to deemed cost of PPE (being previous GAAP carrying amount) for items such as foreign exchange losses on long term monetary items, certain borrowing costs, hedging gains/losses, etc. Companies that have previously reported their first annual financial statements under Ind AS should evaluate the impact of this clarification on their financial results.

- **Accounting for loan and processing fees paid in a refinancing arrangement:** The clarification provided by ITFG relates to an arrangement for refinancing of a loan by a borrower to avail of more advantageous terms. However, this accounting treatment may not apply to situations where the contractual terms of a loan are modified/restructured due to financial difficulties. Companies would have to analyse the relevant facts and circumstances to determine whether the modified loan should be derecognised and the consequent impact on costs and fees incurred in relation to the origination or modification of the loan.



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Tel: +91 22 3989 6000
Fax: +91 22 3983 6000

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
Bund Garden
Vadodara 390 007
Tel: +91 0265 235 1085/232 2607/232 2672

Ahmedabad
Commerce House V, 9th Floor
902 & 903, Near Vodafone House
Corporate Road, Prahaladnagar
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
KRM Tower, Ground Floor,
No 1, Harrington Road
Chetpet, Chennai – 600 031
Tel: +91 44 3914 5000
Fax: +91 44 3914 5999

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

Noida
Unit No. 501, 5th Floor,
Advant Navis Business park
Tower-B, Plot# 7, Sector 142,
Expressway Noida, Gautam Budh Nagar,
Noida – 201305
Tel: +91 0120 386 8000
Fax: +91 0120 386 8999

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

You can reach out to us for feedback and questions at:
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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.

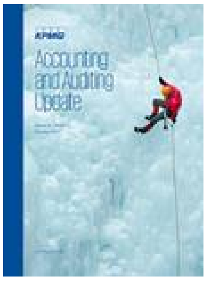
Voices on Reporting

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.

In our recent call on, 4 October 2017, we covered key financial reporting and regulatory matters that are expected to be relevant for stakeholders for the quarter ended 30 September 2017.

Our call included updates from the Ministry of Corporate Affairs (MCA), the Securities and Exchange Board of India (SEBI) and the Institute of Chartered Accountants of India (ICAI).

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



Issue no. 15/2017 – October 2017

In this edition of Accounting and Auditing Update (AAU), we describe the key components of a PD-based approach for computation of ECL on term loans given by financial institutions.

The article on Companies Act, 2013 provides an overview of the requirements of revision or reopening of financial statements and the board's report under the 2013 Act.

This publication also carries an article which elaborates the disclosures that entities should provide when they recognise an impairment loss. Under Ind AS, if there is an indication of impairment then an entity has to perform an impairment test for its non-financial assets such as property, plant and equipment, intangible assets, and its investment in subsidiaries, associates and joint ventures.

The Institute of Chartered Accountants of India (ICAI) published an educational material on Ind AS 18, *Revenue* in the form of frequently asked questions. An article on this topic explains the key principles discussed in the education material.

Our publication also carries a regular synopsis of some recent regulatory updates in India and internationally along with an overview of the report of the Committee on Corporate Governance issued on 5 October 2017.

ICAI issues exposure drafts of AS 23, *Borrowing Costs* and AS 24, *Related Party Disclosures*

1 November 2017

On 5 October 2017, the ASB of the ICAI issued Exposure Drafts (EDs) of the following AS:

- AS 23, *Borrowing Costs*
- AS 24, *Related Party Disclosures.*

This issue of First Notes provides an overview of guidance contained in the ED of AS 23 and ED of AS 24. The note also highlights the areas of key difference between the EDs and the currently applicable AS (i.e. AS 16, *Borrowing Costs*, and AS 18, *Related Party Disclosures* respectively).

It is important to note that ED of AS 23 and AS 24 is not identical to Ind AS 23, *Borrowing Costs* and Ind AS 24, *Related Party Disclosures* respectively. Therefore, this First Notes also highlights additional requirements contained in Ind AS 23 and Ind AS 24.

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