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IFRS Notes

Ind AS Transition Facilitation Group (ITFG) issues Clarifications Bulletin 13

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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 Clarifications' Bulletin 13 on 16 January 2018 to provide clarifications on 10 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, ICAI, on 11 January 2016 announced the formation of the ITFG in order to provide clarifications on issues raised by preparers, users and other stakeholders, related to the applicability and/or implementation of Ind AS under the Companies (Indian Accounting Standards) Rules, 2015 (Ind AS Rules).

Since then, ITFG issued 12 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 13.

Overview of the clarifications in ITFG's Bulletin 13

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

- **Dividend Distribution Tax (DDT):** The ITFG considered certain issues relating to the recognition and accounting for DDT and provided following clarifications in the given cases:

  a) **Capitalisation of DDT as borrowing costs (Issue 1):** Paragraph 8 of Ind AS 23, *Borrowing Costs*, requires an entity to capitalise borrowing costs that are directly attributable to the acquisition, construction or production of a qualifying asset as part of the cost of that asset.

     The ITFG considered a situation in which an entity paid DDT on distribution of dividend to preference shareholders (classified as a liability as per Ind AS 32, *Financial Instruments: Presentation).* The issue considered is whether the DDT could be capitalised as borrowing costs on the qualifying asset in accordance with the principles of Ind AS 23.

     Paragraph 35 of Ind AS 32 states that 'interest, dividends, losses and gains relating to a financial instrument or a component that is a financial liability should be recognised as income or expense in profit or loss. Distributions to holders of an equity instrument should be recognised by the entity directly in equity'. Additionally, paragraph 36 of Ind AS 32 specifies that 'classification of a financial instrument as a financial liability or an equity instrument determines whether interest, dividends, losses and gains relating to that instrument are recognised as income or expense in profit or loss'.

     The ITFG also considered the Guidance Note (GN) on Ind AS Schedule III with respect to 'dividend on redeemable preference shares'. According to the GN, 'the dividend on preferences shares (whether redeemable or convertible) is of the nature of interest expense, only where payment of dividend is not discretionary by the issuer. In such a case, the portion of dividend as determined by applying the effective interest method should be presented as interest expense under 'Finance cost'. Accordingly, the corresponding DDT on such portion of non-discretionary dividends should also be presented in the statement of profit and loss under interest expense'.

     Based on the above guidance, if a financial instrument is classified as **a financial liability**, the **dividend** or interest thereon is in the **nature of interest** which is charged to the statement of profit and loss.

     Therefore, in the given case, the ITFG clarified that subject to meeting the requirements for capitalisation as given in paragraph 8 of Ind AS 23, the dividend on the preference shares (classified as liability as per Ind AS 32) would be treated as interest. The DDT paid thereon would be treated as a cost eligible for capitalisation as it is in the nature of incremental cost that an entity incurs in connection with obtaining the funds for a qualifying asset. Hence, DDT should be capitalised along with interest in the present case. Additionally, the DDT on such dividend will form part of the Effective Interest Rate (EIR) calculation to compute effective interest expense to be capitalised with the qualifying asset.

Overview of the clarifications in ITFG's Bulletin 13 (cont.)

b) **Accounting treatment for DDT in Consolidated Financial Statements (CFS) in case of partly-owned subsidiary (Issue 9):** The ITFG considered the accounting treatment for DDT paid, in the CFS of a company (H Ltd.) holding 60 per cent of the shares (12,000 shares) in its subsidiary (S Ltd.) in the following scenarios:

Scenario 1: S Ltd. paid a dividend at the rate of INR10 per share and DDT at the rate of 20 per cent.

Clarification: The ITFG clarified that in such a situation, dividend income earned by H Ltd. (i.e. INR1,20,000 (12,000 shares*INR10)) and dividend recorded by S Ltd. in its equity (i.e. dividend paid to H Ltd. INR1,20,000) would be eliminated in the CFS of the holding company (i.e. H Ltd.) as a result of a consolidation adjustment. Dividend paid by S Ltd. to the Non-Controlling Interest (NCI) shareholders (i.e. INR80,000 (8,000 shares*INR10)) would be recorded in the statement of changes in equity as a reduction in the NCI balance (as the shares are classified as equity as per Ind AS 32).

Further, ITFG clarified that the DDT paid to tax authorities by S Ltd. (i.e. INR40,000 (2,00,000 shares*20 per cent)) has two components i.e. DDT paid in relation to H Ltd. and DDT paid in relation to NCI.

Accordingly, accounting to be followed is given below:

i. *DDT relating to H Ltd. shareholding (*i.e. INR24,000 (INR40,000*60 per cent)): Charge as tax expense in the consolidated statement of profit and loss of H Ltd. since this is DDT paid outside the group.

ii. *DDT relating to NCI (i.e.* INR16,000 (INR40,000*40 per cent)): Recognise in the statement of changes in equity along with dividend of S Ltd.

It is important to note that ITFG in its bulletin 9 dated 16 May 2017 considered a similar situation where a *wholly-owned subsidiary* paid dividend to its parent and DDT thereon to tax authorities. In that case, ITFG clarified that the dividend income earned by the holding company from its wholly-owned subsidiary and the dividend recorded by the wholly-owned subsidiary should be eliminated as a consolidation adjustment. DDT paid outside the consolidated group i.e. to tax authorities would be charged as an expense in the consolidated statement of profit and loss.

Therefore, ITFG clarified that a similar accounting treatment as given in ITFG bulletin 9 would be applicable in case of a partly-owned subsidiary as well.

The following table depicts these adjustments in the CFS of H Ltd.:

Transactions	H Ltd.	S Ltd.	Consol adjustments	CFS of H Ltd.
Dividend				
Statement of profit and loss (income)	120,000	-	(120,000)	-
Statement of changes in equity by way of reduction of NCI	-	(200,000)	120,000	(80,000)
DDT				
Statement of changes in equity by way of reduction of NCI	-	(40,000)	24,000	(16,000)
Statement of profit and loss	-	-	(24,000)	(24,000)

(Source: ICAI-ITFG Clarifications' Bulletin 13 dated 16 January 2018)

Scenario 2: Dividend and DDT paid by H Ltd.

i. In addition to scenario 1 above, H Ltd. (parent company) also pays dividend of INR300,000 to its shareholders and its DDT liability amounts to INR60,000 (i.e. 20 per cent of INR300,000). However, DDT paid by S Ltd. (i.e. 24,000 as given above) is allowed as set-off against DDT liability of H Ltd. as per the tax laws. Therefore, H Ltd. would be required to pay INR36,000 (INR60,000-INR24,000) as DDT to the tax authorities.

Clarification: If DDT paid by the subsidiary S Ltd. is allowed as a set off against the DDT liability of its parent H Ltd. (as per the tax laws), then the amount of such DDT should be recognised in the consolidated statement of changes in equity of parent H Ltd.

In the given case, share of H Ltd. in DDT paid by S Ltd. is INR24,000 and entire INR24,000 was utilised by H Ltd. while paying dividend to its own shareholders.

Overview of the clarifications in ITFG's Bulletin 13 (cont.)

Accordingly, DDT of INR76,000 (INR40,000 of DDT paid by S Ltd. (of which INR16,000 is attributable to NCI) and INR36,000 of DDT paid by H Ltd.) should be recognised in the consolidated statement of changes in equity of parent H Ltd. Nothing will be charged to consolidated statement of profit and loss.

The basis for such accounting would be that due to parent H Ltd.'s transaction of distributing dividend to its shareholders (a transaction recorded in parent H Ltd.'s equity) and the related DDT set-off, this DDT paid by the subsidiary is effectively a tax on distribution of dividend to the shareholders of the parent company.

The following table depicts the above mentioned treatment in the CFS of H Ltd.:

Transactions	H Ltd.	S Ltd.	Consol adjustments	CFS of H Ltd.
Dividend				
Statement of profit and loss (income)	120,000	-	(120,000)	-
Statement of changes in equity	(300,000)	(200,000)	120,000	(380,000)[1]
DDT				
Statement of changes in equity	(36,000)	(40,000)	-	(76,000)[1]

([1]Dividend of INR80,000 and DDT of INR16,000 will be reflected as reduction from NCI.)

(Source: ICAI-ITFG Clarifications Bulletin 13 dated 16 January 2018)

ii. Modifying scenario 2 in (i) above, H Ltd. pays dividend amounting to INR100,000 with DDT liability of INR20,000 (INR100,000*20 per cent) (instead of dividend of INR300,000 and DDT liability of INR60,000).

Since only INR20,000 has been utilised by H Ltd. out of its share in DDT paid by S Ltd. (i.e. INR24,000), the ITFG clarified that the balance amount (i.e. INR4,000) should be charged to consolidated statement of profit and loss.

The following table depicts the above mentioned treatment in the CFS of H Ltd.:

Transactions	H Ltd.	S Ltd.	Consol adjustments	CFS of H Ltd.
Dividend				
Statement of profit and loss (income)	120,000	-	(120,000)	-
Statement of changes in equity	(100,000)	(200,000)	120,000	(180,000)[2]
DDT				
Statement of changes in equity	-	(40,000)	4,000	(36,000)[2]
Statement of profit and loss	-	-	(4,000)	(4,000)

([2]Dividend of INR80,000 and DDT of INR16,000 will be reflected as reduction from NCI.)

(Source: ICAI-ITFG Clarifications Bulletin 13 dated 16 January 2018)

Scenario 3: DDT has been paid by an associate to its investor. The DDT paid by the associate is not allowed to be set-off against the DDT liability of the investor.

Since the DDT paid by an associate is not allowed to be set-off against the DDT liability of the investor, ITFG clarified that the investor's share of DDT would be accounted by the investor company by crediting its investment account in the associate and recording a corresponding debit adjustment towards its share of profit or loss of the associate.

- **Accounting for a financial guarantee received by a company from its director (Issue 2):** As per Ind AS 109, *Financial Instruments*, a financial guarantee contract is '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'.

  The ITFG considered a situation where a director of a company has provided a guarantee for a term loan to a bank.

Overview of the clarifications in ITFG's Bulletin 13 (cont.)

As per the terms of the loan, the director would be required to compensate for the loss that the bank may incur in case of default by the company. However, the company does not pay premium or fees to its director for providing such financial guarantee. The issue considered relates to whether the company is required to account for the financial guarantee received from its director.

The ITFG considered the definition of a financial guarantee contract (as given in Ind AS 109) and clarified that an evaluation is required to ascertain whether the contract between a director and the bank qualifies as a financial guarantee contract. According to ITFG, in the given case, the contract does qualify as a financial guarantee contract on the following basis:

a) The reference obligation is a debt instrument (i.e. term loan)

b) The holder i.e. bank B is compensated only for a loss that it incurs (arising on account of non-repayment) and

c) The holder is not compensated for more than the actual loss incurred.

However, Ind AS 109 does not specifically address the accounting for financial guarantees by the beneficiary. In an arm's length transaction between unrelated parties, the beneficiary of the financial guarantee would recognise the guarantee fee or premium paid as an expense.

In this case, ITFG clarified that an entity is required to exercise judgement while assessing the substance of the transaction considering the facts and circumstances (such as any other compensation provided to the director for providing this guarantee) based on which an appropriate accounting treatment (on the principles of Ind AS) should be determined.

In the given case, the company is a beneficiary of the financial guarantee and it does not pay a premium or fees (or other compensation) to its director for providing this financial guarantee. Therefore, ITFG clarified that the company would not be required to account for such financial guarantee in its financial statements considering the unit of account as being the guaranteed loan, in which case the fair value is expected to be the face value of the loan proceeds that the company received.

However, paragraph 18 of Ind AS 24, *Related Party Disclosures* requires disclosure of related party transactions during the periods covered by the financial statements, including details of any guarantees given or received by the company. Based on this, the company would be required to make necessary disclosure of the financial guarantee provided by its director.

- **Disclosure of major customers in case of single operating segment (Issue 3):** Ind AS 108, *Operating Segments* is applicable to companies to which Ind AS applies. Paragraph 32 to 35 of Ind AS 108 specify the entity-wide disclosures that an entity is required to make such as revenue from each product and service, information about geographical areas, its major customers, etc.

  Paragraph 34 of Ind AS 108 requires that 'an entity should provide information about the extent of its reliance on its major customers. If revenues from transactions with a single external customer amount to 10 per cent or more of an entity's revenues, the entity should disclose that fact, the total amount of revenues from each such customer, and the identity of the segment or segments reporting the revenues. The entity need not disclose the identity of a major customer or the amount of revenues that each segment reports from that customer.'

  The issue considered relates to whether such a disclosure (of major customers) is required even in case where the company operates only in one segment.

  The ITFG considered the guidance given in paragraph 31 of Ind AS 108 which specifies that 'paragraphs 32 to 34 apply to all entities including those entities that have a single reportable segment'. Accordingly, ITFG clarified that the disclosure requirements as specified in paragraphs 32-34 of Ind AS 108 apply to all entities to which Ind AS applies including entities that have a single reportable segment.

  Therefore, in the given case, information regarding customers contributing to more than 10 per cent of total revenue would have to be disclosed by the company even though it has a single reportable segment. However, the entity need not disclose the identity of a major customer or customers, or the amount of revenues that each segment reports from that customer or those customers.

- **Applicability of NBFC road map to a company performing role of NBFC (Issue 4):** Non-Banking Financial Companies (NBFCs) are required to prepare both consolidated and individual financial statements under Ind AS in two phases commencing from either 1 April 2018 or 1 April 2019 based on certain specified net worth criteria. The issue considered relates to whether Ind AS road map for NBFCs would apply to a company which performs the role of an NBFC and has applied for registration with the Reserve Bank of India (RBI) but is not yet registered as an NBFC.

Overview of the clarifications in ITFG's Bulletin 13 (cont.)

The following is the definition of an NBFC as given under Section 45-I(f) of the Reserve Bank of India (RBI) Act, 1934 (RBI Act). 'An NBFC is a:

a) Financial institution which is a company

b) Non-banking institution which is a company and its principal business is to receive deposits, under any scheme or arrangement or in any other manner, or lending in any manner

c) Such other non-banking institution or class of such institutions, as the RBI may, with the previous approval of the Central Government (CG) and by notification in the official gazette, specify.'

Further, Rule 4(1)(iii) of the Companies (Ind AS) (Amendments) Rules, 2016, defines an NBFC to mean 'a NBFC as defined in Section 45-I(f) of the RBI Act and includes housing finance companies, merchant banking companies, micro finance companies, mutual benefit companies, venture capital fund companies, stock broker or sub-broker companies, nidhi companies, chit companies, securitisation and reconstruction companies, mortgage guarantee companies, pension fund companies, asset management companies and core investment companies'.

The ITFG clarified that the above definition covers a company which is carrying on the activity of an NBFC. Therefore, a company which is carrying on the activity of an NBFC but is not registered with RBI would also be subject to the road map for the applicability of Ind AS, as applicable to any other NBFC.

Additionally, ITFG reiterated that the requirements with regard to registration, eligibility of a company to operate as an NBFC (pending registration), etc. are governed by the RBI Act and rules laid down thereon and therefore, should be evaluated by the company based on its own facts and circumstances.

- **Disclosure of operating profit on the face of statement of profit and loss (Issue 5):** Part II of the Schedule III to the Companies Act, 2013 (2013 Act) specifies the format of the statement of profit and loss of a company and requires, 'revenue from operations' and 'other income' to be shown on the face of the statement of profit and loss.

The general instructions for preparation of statement of profit and loss as given in Schedule III to the 2013 Act provide that 'revenue from operations' should be disclosed separately in the notes as revenue from:

a) Sale of products

b) Sale of services and

c) Other operating revenue.

Similarly, it provides that 'other income' should be classified as:

a) Interest income

b) Dividend income and

c) Other non-operating income (net of expenses attributable to such income).

The ITFG considered whether a company could disclose 'operating profit' on the face of the statement of profit and loss in accordance with Ind AS Schedule III.

The GN on Ind AS Schedule III states that 'the term 'other operating revenue' is not defined. This would include revenue arising from a company's operating activities, i.e., either its principal or ancillary revenue generating activities, but which is not revenue arising from sale of products or rendering of services. Whether a particular income constitutes 'other operating revenue' or 'other income' is to be decided based on the facts of each case and detailed understanding of the company's activities.'

Based on the above, ITFG clarified that disclosure of income should be governed by the GN on Ind AS Schedule III. The Ind AS Schedule III sets out the minimum requirements for disclosure in the financial statements including notes. It states that line items, sub-line items and sub-totals may be presented as an addition or substitution on the face of the financial statements when such presentation is relevant to the understanding of the company's financial position or performance or to cater to industry/sector-specific disclosure requirements, apart from, when required for compliance with amendments to the 2013 Act or Ind AS. Application of such a requirement is a matter of professional judgement as per the GN on Ind AS Schedule III.

The method of computation adopted by the companies for presenting such measures should be followed consistently along with appropriate disclosures relating to the policy followed in the measurement of such line items.

Since certain items which are credited to the statement of profit and loss may not form part of operating profit measure, ITFG clarified that a separate line item for disclosure of the operating profit may not be appropriate and would result in change in the format of statement of profit and loss as prescribed by Schedule III applicable to Ind AS companies.

Additionally, it is important to note that the operating profit measure sub-total would result in a more appropriate presentation of performance for entities which classify expenses by function.

Overview of the clarifications in ITFG's Bulletin 13 (cont.)

However, Ind AS requires classification of expenses by nature and not by function.

Therefore, in the present case, ITFG clarified that it may not be appropriate to present an operating profit measure sub-total as part of the statement of profit and loss. However, the entity may provide such additional information in the financial statements.

- **Timing of recognition of renegotiation gain/loss (Issue 6):** The ITFG considered a situation where there has been a renegotiation of terms of (defaulted) borrowings subsequent to the year end, but before the date of approval of financial statements. The issue considered is whether the modification gain/loss should be recognised in the current year financial statements or in the next year when the terms of (defaulted) borrowings have been renegotiated, in accordance with Ind AS 109.

  The ITFG considered guidance given in paragraph 5.4.3 of Ind AS 109 which states that 'when the contractual cash flows of a financial asset are renegotiated or otherwise modified and the renegotiation or modification does not result in the derecognition of that financial asset in accordance with Ind AS 109, then an entity should recalculate the gross carrying amount of the financial asset and should recognise a modification gain or loss in profit or loss'.

  Based on the above, ITFG clarified that modification gain or loss should be recognised in profit or loss in the period in which the renegotiation contractually takes place. Therefore, in the given case, if the terms of the (defaulted) borrowings have been renegotiated in the next year, then the related gain/loss should also be recognised in the next year.

- **Accounting for partial disposal of an investment in a subsidiary (Issue 7):** The ITFG considered a situation in which a parent holds 70 per cent shares in its subsidiary. However, due to additional funds invested by the other investor, the parent's stake reduced to 60 per cent with no subsequent loss of control by the parent.

  The issue raised relates to how this partial deemed disposal should be accounted:

  - In the separate financial statements of the parent considering that investment in the subsidiary is measured at cost.
  - In the CFS.

  The ITFG prescribes following accounting treatment in case of:

  a) **Separate financial statements of the parent:** There would be no impact and investment in subsidiary would continue to be recognised at its carrying amount. However, the parent should disclose the fact that the shareholding has been reduced from 70 per cent to 60 per cent in its separate financial statements.

  b) **CFS**: Paragraph 23 of Ind AS 110, *Consolidated Financial Statements* specifies that changes in a parent's ownership interest in a subsidiary that do not result in the parent losing control of the subsidiary are equity transactions (i.e. transactions with owners in their capacity as owners). Therefore, such transactions do not have any impact on goodwill or the statement of profit and loss.

     Paragraph B96 of Appendix B to Ind AS 110 provides that when the proportion of the equity held by NCI changes, an entity should adjust the carrying amounts of the controlling and non-controlling interests to reflect the changes in their relative interests in the subsidiary. Any difference between the amount by which the NCI are adjusted and the fair value of the consideration paid or received should be recognised directly in equity and should be attributed to the owners of the parent.

     Further, ITFG highlighted that NCI are recorded at fair value (or proportionate share in the recognised amounts of the acquiree's identifiable net assets, if chosen) only at the date of the business combination. Subsequent purchases or sales of ownership interests when control is maintained are recorded at the NCI's proportionate share of the net assets.

     Additionally, the entity would be required to present a schedule that shows the effects of changes in ownership interest on the equity attributable to owners of the parent.

- **Disclosure of foreign currency risk (Issue 8):** As per paragraph D13AA of Ind AS 101, *First-time Adoption of Ind AS,* a first-time adopter may continue to apply its previous GAAP policy adopted for accounting for exchange differences arising from translation of long-term foreign currency monetary items recognised in the financial statements for the period ending immediately before the beginning of the first Ind AS financial reporting period.

  The ITFG considered a situation where a company has availed the option in Ind AS 101 (paragraph D13AA) and capitalised the foreign exchange differences. The issue is whether the foreign currency risk disclosure of Ind AS 107, *Financial Instruments: Disclosures* would apply to such foreign exchange differences.

Overview of the clarifications in ITFG's Bulletin 13 (cont.)

Paragraph 40(a) of Ind AS 107 requires an entity to disclose a sensitivity analysis for each type of market risk (including foreign currency risk) to which the entity is exposed at the end of the reporting period, showing how profit or loss and equity would have been affected by changes in the relevant risk variable that were reasonably possible at that date.

Based on the above, ITFG clarified that if a company capitalises foreign exchange differences in the cost of a related asset, then the company is exposed to foreign currency risk on this exposure and there could be an indirect impact in the profit and loss or equity, for example through depreciation.

Accordingly, in the given case, it has been clarified that the company should provide appropriate disclosures where applicable under Ind AS 107 even though the company has availed the option under paragraph D13AA of Ind AS 101.

- **Computation of financial liability in a compound financial instrument (Issue 10):** The ITFG considered a situation where a company has issued compulsorily convertible debentures at 14.5 per cent coupon rate convertible at the end of 10 years. The coupon rate on debentures is same as that of the market rate of interest i.e. 14.5 per cent. Further, the equity conversion option requires the company to deliver a fixed number of its own shares for a fixed amount of another financial asset indicating that it meets the 'fixed for fixed' criterion under Ind AS 32.

  The ITFG considered how the financial liability (debt portion) would be computed in such a situation.

  Ind AS 32, *Financial Instruments: Presentation* (paragraph 28 to 32) requires that a compound financial instrument should be separated into its components: financial liability (i.e. debt) and equity component. Further, it provides that while allocating the initial carrying amount of the compound instrument to the underlying financial liability and equity component, an entity should first determine the fair value of the liability component (assuming there is no embedded derivative).

  The fair value of the liability component is determined with reference to the fair value of a similar stand-alone debt instrument. Accordingly, the amount allocated to the equity component is the residual amount after deducting the fair value of the financial liability component from the fair value of the entire compound instrument.

  The ITFG also considered the application guidance of Ind AS 32 (paragraph AG31 of Appendix A) which states that a common form of compound financial instrument is a debt instrument with an embedded conversion option, such as a bond convertible into ordinary shares of the issuer, and without any other embedded derivative features. An issuer of such a financial instrument should present the liability component and the equity component separately in the balance sheet, as follows:

  a) The issuer's obligation to make scheduled payments of interest and principal is a *financial liability* that exists as long as the instrument is not converted.

     On initial recognition, the fair value of the liability component is the present value of the contractually determined stream of future cash flows discounted at the rate of interest applied at that time by the market to instruments of comparable credit status and providing substantially the same cash flows, on the same terms, but without the conversion option.

  b) The *equity instrument* is an embedded option to convert the liability into equity of the issuer. This option has value on initial recognition even when it is out of the money.

  On the basis of the above guidance, ITFG clarified that in the given case, the fair value of the liability should be computed as the present value of the contractually determined stream of future cash flows discounted at the rate of interest applied at that time by the market to instruments of comparable credit status and providing substantially the same cash flows, on the same terms, but without the conversion option.

  Further, the amount allocated to the equity component will be the residual amount after deducting the fair value of the financial liability component as determined above from the fair value of the entire compound instrument (transaction costs have been ignored in this case).

Our comments

The ITFG clarifications are expected to resolve various practical implementation issues faced by companies that report their financial results 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 specific facts and circumstances.

Specifically, companies may consider the following aspects:

- **Companies operating as NBFCs are required to follow Ind AS road map applicable to NBFCs**: The ITFG clarified that companies which are carrying on the business of NBFCs but are not registered with the RBI as NBFCs are required to follow the Ind AS road map specified for NBFCs i.e. such companies are required to apply Ind AS with effect from 1 April 2018 (transition date 1 April 2017).

  Such companies should therefore, carefully evaluate whether they meet the definition of NBFCs under the RBI Act and if so, commence timely preparation for their transition to Ind AS. Further, their holding, subsidiary, associate or joint venture companies, which were not covered under the corporate road map would also need to prepare Ind AS based financial statements based on the road map applicable to NBFCs.

- **Dividend paid to preference shareholders qualifies as interest and DDT thereon eligible for capitalisation**: Subject to meeting the requirements of Ind AS 23, ITFG clarified that the dividend paid on preference shares that are classified as a financial liability as per Ind AS 32, qualifies as an interest expense. Further, the DDT paid on such dividends is eligible to be capitalised along with the interest as it is in the nature of incremental cost that an entity incurs in connection with obtaining the funds for a qualifying asset.

  This clarification is therefore expected to be relevant to companies that have preference share liabilities (to raise funds for acquisition of a qualifying asset) and have incurred DDT liability on dividend paid to preference shareholders.

  Further clarity may be required on the accounting treatment for companies that have already transitioned to Ind AS but have not considered such DDT as part of borrowing costs in their annual Ind AS financial statements for the financial year 2016-17.

- **Market risk includes foreign exchange risk**: In its third clarifications' bulletin, ITFG opined that an entity that has availed of the option available under paragraph D13AA of Ind AS 101 and continues to capitalise (to the cost of the related asset) the foreign exchange differences arising from a long-term foreign currency loan, has no corresponding foreign currency exposure (arising from that loan) that affects profit or loss. Accordingly, cash flow hedge accounting under Ind AS 109 would not apply to any foreign currency derivatives transacted to hedge the foreign currency risk of such loans. Such derivatives would therefore be recognised at fair value through profit or loss.

  In Bulletin 13, ITFG opined that a company that avails the option under paragraph D13AA of the Ind AS 101 and continues to capitalise foreign exchange differences on long-term foreign currency monetary items remains exposed to foreign currency risk. Further, this risk is expected to affect profit or loss indirectly (e.g., in the form of depreciation) in the future. Therefore, such a company would be required to provide foreign currency risk related disclosures under Ind AS 107.

  This view seems to support the applicability of hedge accounting in a situation where foreign currency derivatives have been transacted to mitigate currency risk on long-term foreign currency monetary items for which an entity continues the policy of capitalising foreign currency differences. The ITFG may consider providing further clarification to this effect.

- **Disclosure of operating profit**: The ITFG has clarified that it may not be appropriate to present an 'operating profit' measure sub-total as part of the statement of profit and loss as the format of statement of profit and loss is based on nature of expenses. However, a company that would like to present this measure may consider disclosing 'operating profit' as an additional information in the notes to its financial statements and not on the face of the statement of profit and loss. Under International Accounting Standard (IAS 1), *Presentation of financial statements,* companies would have the option to present 'operating profit' as an additional sub-total as part of the statement of profit and loss as IAS 1 allows use of format where expenses can be categorised by function (i.e. under International Financial Reporting Standards (IFRS), expenses recognised in the statement of profit and loss are classified according to their nature or function).

KPMG in India

Hyderabad
Salarpuria Knowledge City,
ORWELL, 6th Floor, Unit 3, Phase III,
Sy No. 83/1, Plot No 2,
Serilingampally Mandal, Raidurg
Ranga Reddy District,
Hyderabad, Telangana – 500081
Tel: +91 40 6111 6000
Fax: +91 40 6111 6799

Kochi
Syama Business Centre
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

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

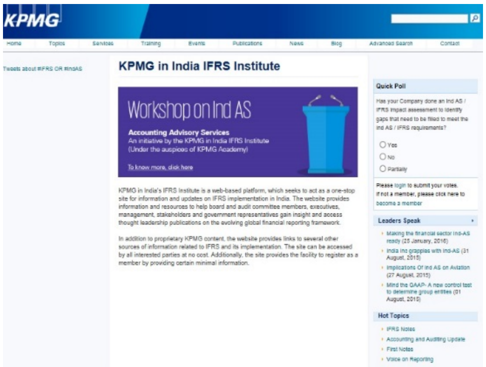
Gurugram
Building No.10, 8th Floor
DLF Cyber City, Phase II
Gurugram, Haryana 122 002
Tel: +91 124 307 4000
Fax: +91 124 254 9101

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:
in-fmkpmgifrsinst@kpmg.com

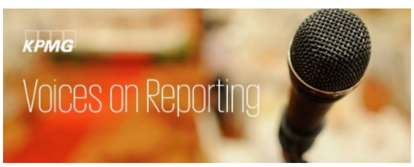
KPMG in India's IFRS institute



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



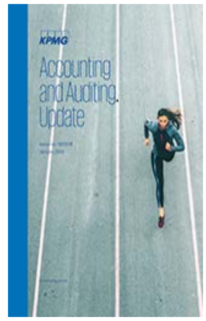
KPMG in India is pleased to present Voices on Reporting – a monthly series of knowledge sharing calls to discuss current and emerging issues relating to financial reporting.

The new revenue standard (Ind AS 115, *Revenue from Contracts with Customers*) is expected to be applicable to Indian companies following the Ind AS road map framework from 1 April 2018.

Starting from January 2018, the Voices on Reporting presents a series of special sessions to discuss insights on Ind AS 115.

In the first session of Ind AS 115 series held on 17 January 2018, we discussed the key requirements of Ind AS 115, transition and key impact areas.

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



Issue no. 18/2018 – January 2018

IThe Companies Act, 2013 (2013 Act) has been operationalised by the Ministry of Corporate Affairs (MCA) from 1 April 2014. Over the past three years, MCA has issued a number of amendments and clarifications to various sections and rules of the 2013 Act.

On 3 January 2018, the Companies (Amendment) Act, 2017 received the assent of the President of India. The Companies (Amendment) Act, 2017 makes significant changes to the 2013 Act which aim at ease of doing business, better corporate governance and enforcement of stringent penal provisions for defaulting companies.

The Companies (Amendment) Act, 2017 will come into effect on such date as the Central Government (CG) may, by notification in the Official Gazette, appoint. Different dates may be appointed for different provisions of the 2013 Act and any reference in any provision to the commencement of the 2013 Act should be construed as a reference to the coming into force of that provision.

This month's issue of the Accounting and Auditing Update (AAU) contains an updated compilation of our articles over the last year on the key aspects of the 2013 Act.

These articles include clarifications and implementation related insights that have been gained as companies have sought to apply in practice this legislation, including changes made by the Companies (Amendment) Act, 2017. Our publication also carries a regular synopsis of some recent regulatory updates in India and internationally.

SEBI relaxes norms governing schemes of arrangements by listed entities

18 January 2018

The listed entities that desire to undertake a scheme of arrangement or are involved in a scheme of arrangement need to follow the regulations laid down by the Securities and Exchange Board of India (SEBI). On 10 March 2017, SEBI issued a circular number CFD/DIL3/CIR/2017/21 which laid down a revised regulatory framework for schemes of arrangements by listed entities and relaxation under Rule 19(7) of the Securities Contract (Regulation) Rules, 1957.

The SEBI received representations to improve the existing framework governing schemes of arrangements.

Additionally, SEBI wanted to expedite the processing of draft schemes and prevent misuse of schemes to bypass regulatory requirements. Therefore, on 3 January 2018, SEBI issued a circular number CFD/DIL3/CIR/2018/2 (the circular) to make certain amendments to the circular dated 10 March 2017.

The recent circular is applicable from the date of its issue i.e. 3 January 2018. In this issue of First Notes, we have provided an overview of the key amendments/relaxations given in the circular.

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