KPMG

IFRS Notes

MCA notifies amendments to the consolidation exception for investment entities

19 April 2016

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Introduction

On 30 March 2016, the Ministry of Corporate Affairs (MCA) notified the Companies (Indian Accounting Standards) (Amendments) Rules, 2016 (Ind AS), which included amendments to the following standards:

- Ind AS 110, *Consolidated Financial Statements*
- Ind AS 112, *Disclosure of Interests in Other Entities,* and
- Ind AS 28, *Investments in Associates and Joint Ventures.*

These amendments provide additional guidance and clarity when applying the consolidation exception for investment entities. They are based on identical amendments that were made to the corresponding International Financial Reporting Standards (IFRS) in December 2014, which are applicable for accounting periods beginning on or after 1 January 2016 internationally.

The Ind AS amendments would apply from accounting periods beginning from 1 April 2016 onwards and shall result in convergence with the currently applicable IFRS.

"The MCA amendments to Ind AS 110, Ind AS 112 and Ind AS 28 are in line with similar amendments to IFRS internationally. These are intended to resolve practical challenges for investment entities in implementing the exception to consolidation requirements and are expected to be relevant to groups that include entities such as venture capital funds, private equity funds, core investment companies and such others."

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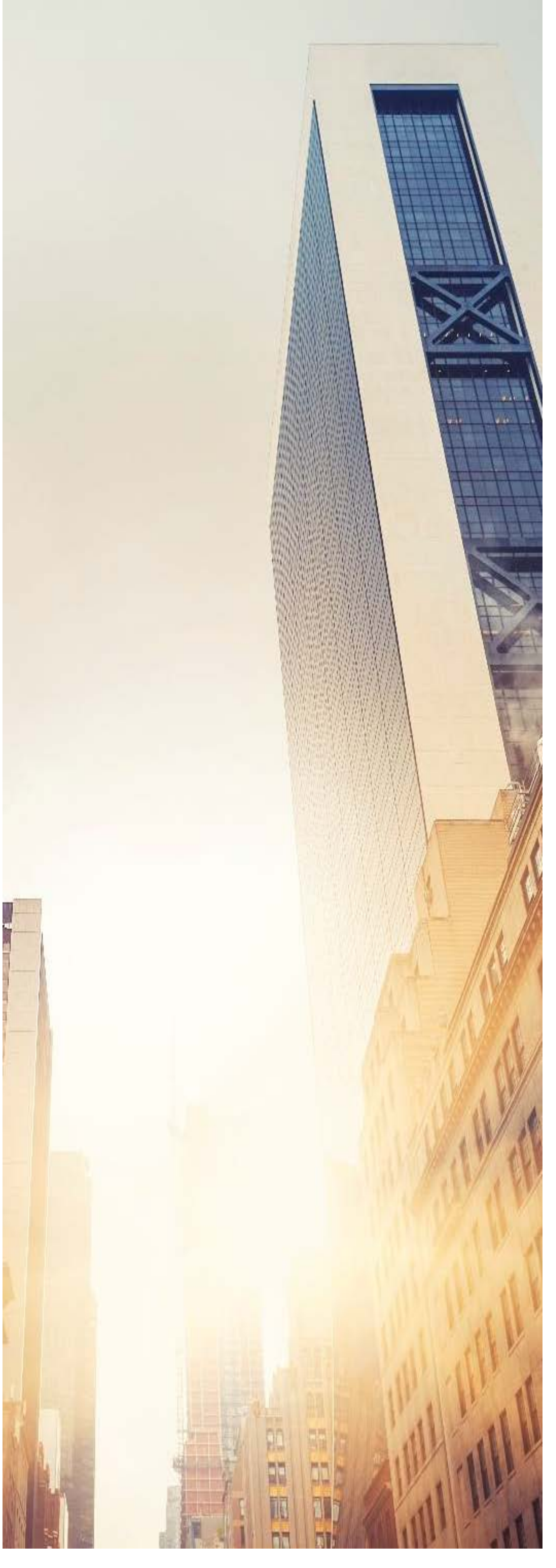


Background

Currently under Ind AS, investment entities are exempt from consolidating their subsidiaries and are required to measure such an investment at fair value through profit or loss (as per Ind AS 109, *Financial Instruments*). Investment entities are also required to measure their investments in associates and joint ventures at fair value through profit or loss.

However, there was some uncertainty surrounding the interpretation of this consolidation exception in certain circumstances, when applied in practice internationally. These amendments address those situations and are expected to reduce diversity in practice.

Overview of the amendments

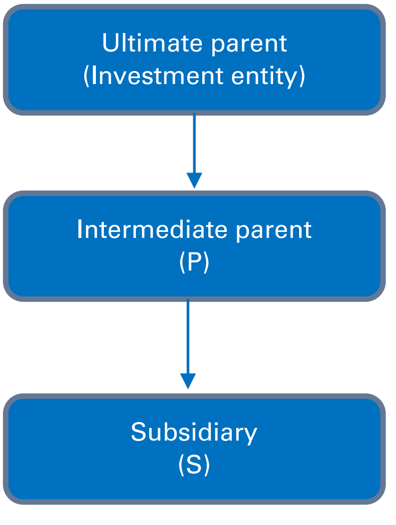
Ind AS 110

Consolidation exception for intermediate parents owned by investment entities

The standard provides an exemption to a parent from preparing consolidated financial statements if certain conditions are fulfilled. One of the conditions is that its ultimate or intermediate parent produces consolidated financial statements that are available for public use and comply with Ind AS.

The amendment addresses the question whether the above exemption is available to a parent entity that is a subsidiary of an ultimate, or an intermediate, investment entity parent as the investment entity parent does not consolidate any of its subsidiaries. Instead, the investment entity parent prepares financial statements in which all of its subsidiaries are measured at fair value through profit or loss. This amendment clarifies that the exemption from consolidation will also be available if an entity's ultimate or intermediate parent's financial statements include subsidiaries that are not consolidated and are measured at fair value through profit or loss in accordance with Ind AS 110.

This is illustrated in Figure 1 below:



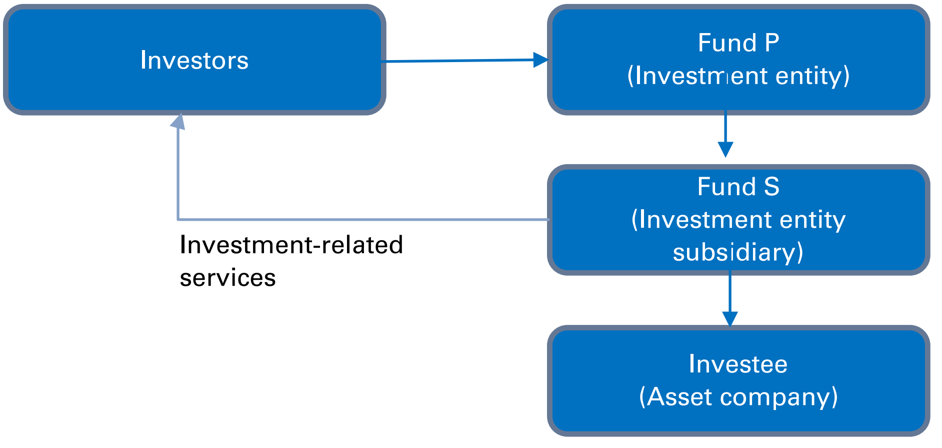
In this example, the intermediate parent 'P' need not present consolidated financial statements since its investment entity parent produces financial statements in which it measures its interest in its subsidiaries (including P) at fair value through profit or loss.

Consolidation exception for investment entity subsidiary providing investment related services

Previously, it was unclear whether an investment entity should consolidate a subsidiary that carries out investment related services or activities even when such subsidiary qualifies as an investment entity itself. Internationally, this led to diversity in practice when accounting for such subsidiaries.

The amendments to Ind AS 110 clarify that:

- An investment entity is required to consolidate only non-investment entity subsidiaries (subsidiaries that do not meet the definition of an investment entity under Ind AS 110) whose main purpose and activities are to provide investment-related services.
- An investment entity is required to measure all its investment entity subsidiaries (subsidiaries that meet the definition of an investment entity under Ind AS 110) at fair value through profit or loss, even if such subsidiaries provide investment related services. This is illustrated in Figure 2 below:



In this example, the parent investment entity, Fund P, will not be permitted to consolidate its investment entity subsidiary, Fund S, even though it may provide investment related services that are substantial in nature, to the investors in Fund P, instead Fund P would account for Fund S at fair value through profit or loss.

Ind AS 112

The MCA notification amends Ind AS 112 to clarify that an investment entity that prepares financial statements in which all of its subsidiaries are measured at fair value through profit or loss shall be required to present the disclosures relating to investment entities that are required in Ind AS 112.

Ind AS 28

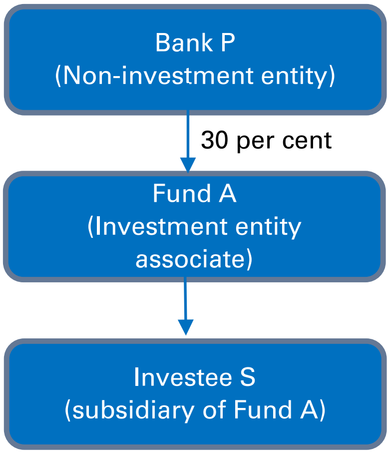
Accounting policy choice for equity accounting of an interest in an investment entity

Previously, Ind AS 28 did not clarify whether a non-investment entity parent that applies the equity method to its investment in an investment entity associate or joint venture, was permitted to retain the fair value measurement of its subsidiaries, which was applied by such associate or joint venture in its financial statements. Therefore, the non-investment entity parent would have been required to obtain the consolidated financial statements for its investment entity associate or joint venture (prepared as if the associate or joint venture did not qualify as an investment entity) and apply the equity method based on those consolidated financial statements.

Internationally, this posed a challenge as the investment entity associate or joint venture would not normally have prepared consolidated financial statements since IFRS 10/IndAS 110 required them to recognise investments in their subsidiaries at fair value through profit or loss. It would be burdensome or even impracticable to require the associate or joint venture to prepare a second set of financial information on a consolidated basis solely for the purpose of equity accounting by the parent.

The amendment provides an accounting policy choice and clarifies that a non-investment entity parent that applies the equity method to account for an interest in an associate or joint venture that is an investment entity, may opt to retain the fair value measurement applied to their subsidiaries by such associate or joint venture.

This accounting treatment is illustrated in Figure 3 below:

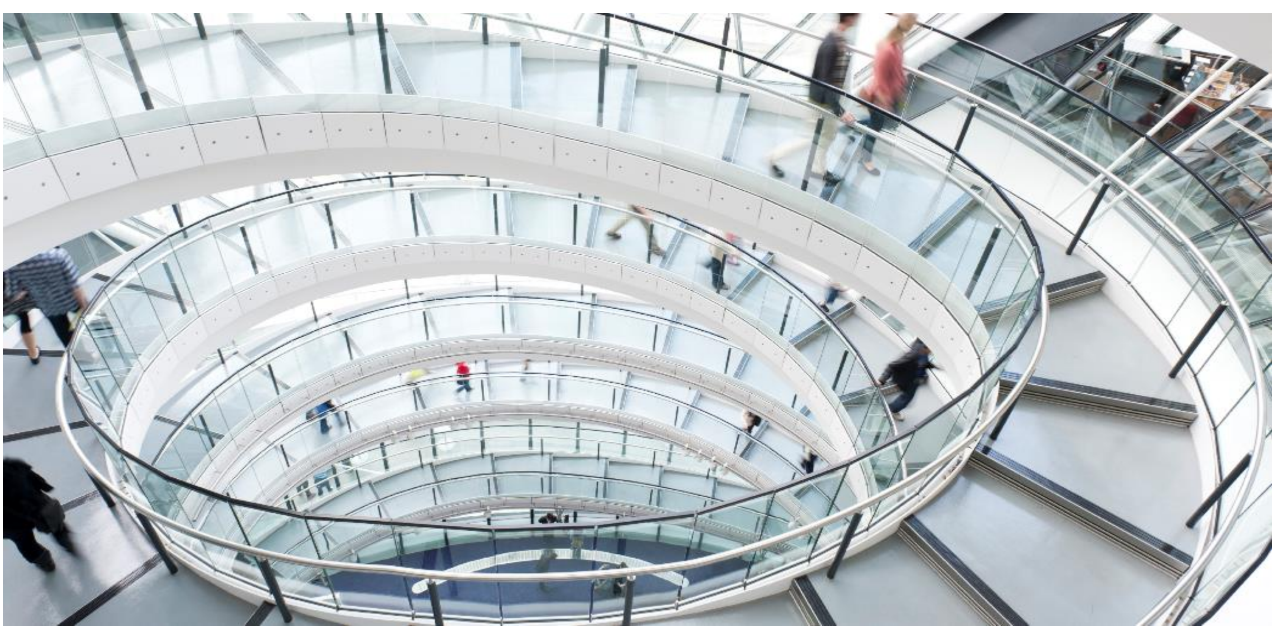


In this example, Fund A is required to measure its interest in the investee company S at fair value through profit or loss as Fund A qualifies as an investment entity. The parent entity Bank P will be required to equity account for its interest in Fund A and has the option to retain the fair value measurement applied by Fund A to entity S. Alternatively, Bank P may continue to apply the equity method by requesting for a set of consolidated financial statements from Fund A.

Our comments

The amendments to Ind AS 110, Ind AS 112 and Ind AS 28 are designed to improve the practical application of the consolidation exception and are in line with the amendments made to IFRS. These amendments are expected to be relevant to investment entities such as private equity funds, venture capital funds, core investment companies, etc. as they transition to Ind AS.

These amendments will also be relevant to entities that have investments in associates or joint ventures that qualify as investment entities.



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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.

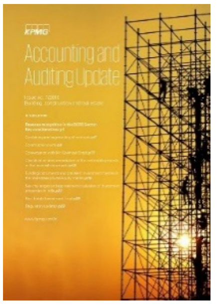
Voices on Reporting

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 call, on 5 April 2016, we covered key financial reporting and regulatory matters that are expected to be relevant for stakeholders for the financial year ending 31 March 2016.

Our call included updates from the Ministry of Corporate Affairs (MCA), the Securities and Exchange Board of India (SEBI), the Reserve Bank of India (RBI), the Institute of Chartered Accountants of India (ICAI), the Insurance Regulatory and Development Authority of India (IRDA), etc.

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



The Accounting and Auditing Update issue 2016/7 focusses on the Building, Construction and Real Estate (BCRE) sector and highlights key matters relating to accounting, financial reporting and regulatory areas relevant to this sector.

In this publication, we highlight current Indian GAAP guidance on revenue recognition by the sector and the guidance under IFRS. The Institute of Chartered Accountants of India is expected to issue a guidance note to provide direction on the accounting of revenue recognition from the sale of real estate under Ind AS and we have highlighted the potential challenges that may arise due to adoption of Ind AS.

The publication features an interview with Mr. Govinder Singh, International Business Head and Ex-Chief Financial Officer, Tata Housing Development Company Limited, and explores some key accounting, reporting and other topical matters relevant to the industry.

The publication also carries a number of other accounting issues in detail, which are relevant to this sector.

Additionally, our publication carries a regular synopsis of regulatory updates.

The proposed Companies (Amendment) Bill, 2016

1 April 2016

Based on the recommendations of the CLC report, on 16 March 2016, the government proposed the Companies (Amendment) Bill 2016, (the Bill) on issues arising on account of implementation of the Companies Act, 2013 (2013 Act) in the Lok Sabha to amend the 2013 Act. The Bill considered the suggestions made by the CLC as well as the comments received from the stakeholders and ministries/departments.

The recommendations cover significant areas of the 2013 Act, including definitions, raising of capital, accounts and audit, Corporate Social Responsibility (CSR), managerial remuneration, companies incorporated outside India and offences/penalties.

This issue of First Notes summarises key recommendations of the Bill.

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