



# IFRS Notes

**SEBI issues a  
consultation paper on  
disclosure of financial  
information in offer  
document/placement  
memorandum and  
valuation of the units of  
Infrastructure Investment  
Trusts**

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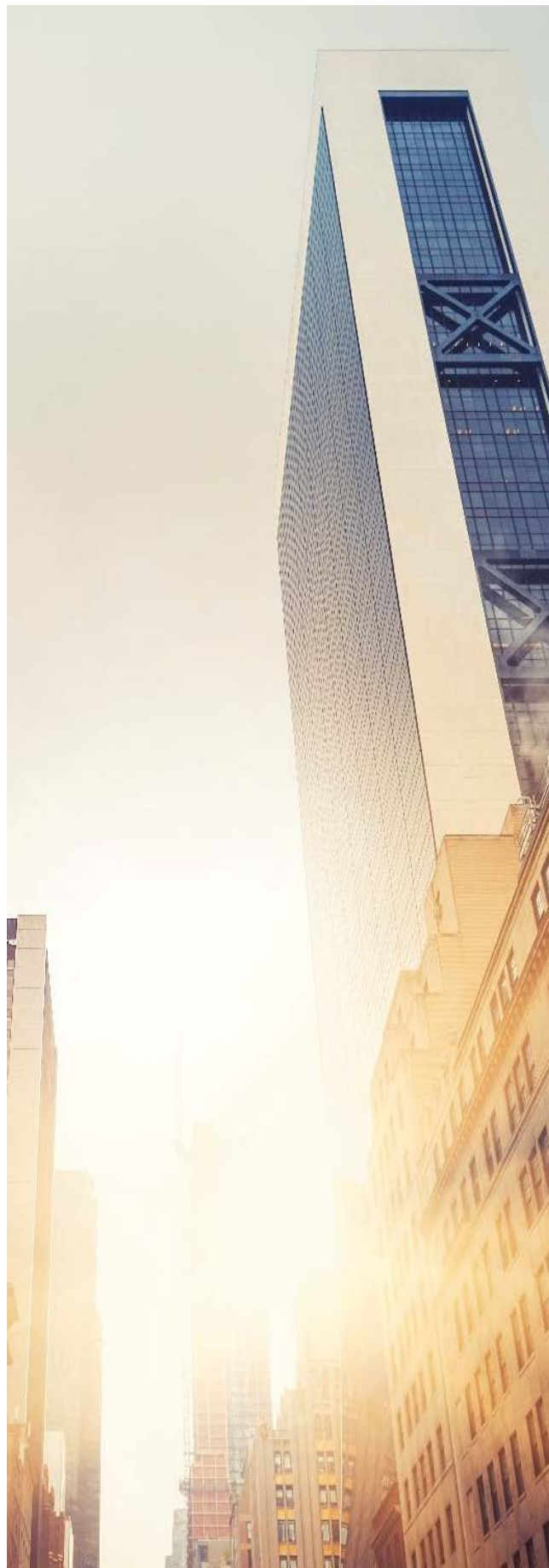


## Introduction

The Securities and Exchange Board of India (SEBI) issued a consultation paper on 15 June 2016, proposing continuous financial disclosures and other continuous disclosures to be made by Infrastructure Investment Trusts (InvITs) registered under the SEBI (Infrastructure Investment Trusts) Regulations, 2014 (InvIT Regulations).

Continuing with its recommendations, SEBI on 8 July 2016, issued a consultation paper proposing the following:

- Guidelines for financial disclosures in the offer document/placement memorandum
- Valuation of the units of InvITs.



**“SEBI’s consultation paper introduces certain international best practices on the disclosure of financial information by InvITs in their offer documents/placement memorandum. While these disclosures may require additional efforts in terms of preparation and audit of the relevant information, they will result in the provision of more meaningful and useful information to potential investors.”**

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## Background

The InvIT Regulations notified on 26 September 2014 prescribe the general conditions for making a public offer and private placement and broad guidelines for making initial and continuous disclosures, including disclosures of financials of the InvIT. Further, SEBI has constituted a Committee (the Committee) consisting of representatives from the Institute of Chartered Accountants of India (ICAI) and the industry to prescribe more specific requirements relating to accounting and auditing norms for InvITs.

Based on the recommendations of the Committee, SEBI issued this consultation paper proposing a framework for disclosures in the offer document/placement memorandum and for valuation of the units of InvIT with a view to ensure comparability, uniformity and parity in disclosures made by InvITs.

## Overview of the proposed framework

### Financial disclosures in the offer document/placement memorandum

The following is an overview of the significant proposals in this section:

#### 1) Annual financial information

Annual financial information for the previous three financial years needs to be disclosed by an InvIT in either of the following manner:

- *If the InvIT has been in existence for the last three financial years:* Historical audited financial statements of the InvIT (on both stand-alone as well as consolidated basis) for the last three years to be disclosed.
  - *If the InvIT has been in existence for less than three financial years:* Audited Combined Financial Statements (as defined below) need to be disclosed for the periods when historical audited financial statements was not available.
- a) Combined Financial Statements:** These comprise of all the assets or entities, which are owned by an InvIT (including assets or entities proposed to be owned by the InvIT prior to allotment of units in the initial offer).
- The combined financial statements should be prepared on a combined basis, using the principles of Ind AS 110, *Consolidated Financial Statements*, and presented as if InvIT assets were a part of the InvIT since the first day of the three year period for which information is being presented.
  - Unlike consolidated financial statements, the combined financial statements would not include the parent. However, transactions between InvIT owned entities should be eliminated from these statements.
  - Where one or more of the underlying InvIT assets have been held for a period of less than the last three financial years, then such assets may be reflected in the combined financial statements from the date of holding. However, if financial information for those assets is available for the pre-holding period, then such assets may be reflected for the pre-holding period as well.
- b) Accounting Standards:** The consultation paper proposes that the annual financial information (either historical or combined financial statements) should be prepared in accordance with the Indian Accounting Standards (Ind AS).
- c) Financial statements and line items:** The consultation paper proposes, at a minimum, the following components for annual and combined financial statements:
- i. Balance sheet
  - ii. Statement of profit and loss
  - iii. Statement of changes in equity
  - iv. Statement of cash flows, and
  - v. Explanatory notes annexed to, or forming part of, any of the above given statements.



Additionally, the consultation paper specifies the minimum line items to be disclosed in the above mentioned components. All 'material' items are required to be disclosed. The consideration of materiality is similar to that defined in Schedule III of the Companies Act, 2013 (the 2013 Act).

**d) Audit of financial information:** The consultation paper provides for audit of the annual financial information and the combined financial statements by the auditor appointed as per the InvIT Regulations.

- The auditor should follow the requirements of the Guidance Note on Reports in Company Prospectuses issued by the ICAI while providing the report.
- The reports of the auditors on the financial statements of the various InvIT assets for the periods covered in the last three years should be considered and relied upon by the auditor. The audit procedures to be followed in such cases should be in line with the procedures stated in the Standard on Auditing (SA) 600, *Using the Work of Another Auditor*.

The consultation paper requires that an auditor should provide an opinion on whether each of the components of the financial statements present a true and fair view.

**e) Additional disclosures:** The consultation paper also proposes the following additional disclosures:

- Operating cash flow from the projects (project-wise) for all InvIT assets for the previous three years.
- Earnings Per Unit (EPU) for the previous three years computed in accordance with Ind AS 33, *Earnings per Share*.
- Market value of the units traded on all the designated stock exchanges where the InvIT is listed, in case of a capital offering subsequent to the initial offer.

## 2) *Interim financial information*

If the date of the draft offer document/offer document/placement memorandum is more than six months from the end of the last audited annual financial statements, an InvIT is required to disclose its audited interim financial information, in addition to the annual financial information.

## 3) *Financial information of manager and sponsor*

The consultation paper proposes that an offer document/placement memorandum of an InvIT shall include a summary of the audited consolidated financial statements (including the balance sheet and statement of profit and loss of a manager and sponsor(s) for the past three years, prepared in accordance with Ind AS and the 2013 Act. However, if the manager and/or the sponsor is required to follow Ind AS only for the latest two years out of the historical period of three years, then financial information for the earliest year is to be disclosed in accordance with the Companies (Accounting Standards) Rules, 2006 (previous Indian Generally Accepted Accounting Principles (GAAP)).

If any of the manager/sponsor is a foreign entity and is not legally required to comply with Ind AS and the 2013 Act, financial statements can be prepared in accordance with the International Financial Reporting Standards (IFRS).

## 4) *Management Discussion and Analysis (MDA)*

The consultation paper proposes that the InvIT should prepare and disclose MDA based on historical financial statements along with providing a comparison for the most recent financial information with financial information of the previous two years. The consultation paper also specifies the minimum line items to be included in the MDA.

## 5) *Projections of revenues and operating cash flows*

The InvIT Regulations require disclosure of projections of revenue and operating cash flows, project-wise over the next three years, including the related assumptions. These projections should be certified by the auditor.

The consultation paper proposes that such projections shall be disclosed for InvIT assets/projects that are owned by the InvIT or are proposed to be owned by InvIT prior to the allotment of units in the public offer/private placement.

#### 6) *Payment history and working capital available to InvIT*

The current InvIT regulations do not provide any guidelines on payment history and computation of working capital available to InvIT.

The consultation paper proposes that a statement regarding sufficiency of the working capital to fulfil the present requirements of the InvIT (i.e. at least 12 months from the date of listing) should be included by the investment manager, along with disclosure of interest and principal payments of an InvIT for the past three years. If sufficient working capital is not available, the investment manager is required to describe how it proposes to provide for additional capital.

#### 7) *Contingent liabilities*

Disclosure of the statement of an InvIT's contingent liabilities, if any, as on the date of the offer document/placement memorandum is required, along with classification of the contingent liabilities into its specified categories.

#### 8) *Commitments*

The consultation paper provides that the commitments as on date should be classified into the following heads, at minimum and disclosed:

- a) Estimated amount of contracts remaining to be executed on capital account and not provided for;
- b) Uncalled liability on shares and other investments partly paid, including that of Special Purpose Vehicle (SPV);
- c) Other commitments (specify nature).

#### 9) *Other disclosures*

- a) **Related party transactions:** In addition to the requirements in the InvIT regulations, an InvIT should also comply with the requirements of Ind AS 24, *Related Party Disclosures* while preparing its financial information. Further, additional minimum disclosures, including details of the related party and its relationship with InvIT, nature and value of the transaction, etc. are to be provided by the InvIT.
- b) **Capitalisation statement:** An InvIT should include a capitalisation statement in the offer document/placement memorandum, showing total debt, net worth, and the debt/equity ratios before and after the completion of issue.

### **Valuation of the units of InvITs**

The following are the significant proposals in the consultation paper relating to valuation of units:

#### 1) *Amendment in the definition of valuer*

##### *Current requirements*

- The current InvIT Regulations define a valuer as any person who is a 'registered valuer' under Section 247 of the 2013 Act and who has been appointed by the investment manager to undertake valuation of the InvIT assets provided that till such date on which Section 247 of the 2013 Act comes into force, a valuer shall mean an independent merchant banker registered with the Board or an independent chartered accountant in practice having a minimum experience of 10 years.

##### *Proposal*

- Based on the representations received from various stakeholders, to expand the definition of a valuer, the Committee has recommended that until such time that Section 247 of the 2013 Act comes into force, the draft rules of the 2013 Act, may be used for defining valuer under the InvIT Regulations.

- Accordingly, a 'valuer' means the person(s) who is/are eligible to apply to be a 'registered valuer' under Section 247 of the 2013 Act, and who have been appointed by the investment manager to undertake valuation of InvIT assets. Until such date on which Section 247 of the 2013 Act comes into force, a valuer shall mean:
  - a) A chartered accountant, company secretary or cost accountant who is in whole-time practice, or a retired member of the Indian Corporate Law Service or any person holding an equivalent Indian or foreign qualification as the Ministry of Corporate Affairs (MCA) may recognise by an order provided that such foreign qualification is acquired by an Indian citizen
  - b) A merchant banker registered with SEBI, and who has in his/her employment, person(s) having qualifications prescribed under (a) above to carry out valuation by such qualified persons
  - c) A member of the Institute of Engineers and who is in whole-time practice
  - d) A member of the Council of Architecture or the Indian Institute of Architects, and who is in whole-time practice
  - e) A person or entity possessing the necessary competence and qualification in valuations as may be notified by the Central Government from time to time.

The consultation paper sets out the minimum requirements for such valuers in terms of continuous experience and membership of the respective institutions. Further, the persons referred to in (a) and (b) above, shall be valuers in respect of a 'financial valuation' and the persons referred to in (c) and (d) shall be valuers for a 'technical valuation' and a person or a firm or a Limited Liability Partnership or a merchant banker possessing both the qualifications may act in dual capacity.

## 2) **Mandatory disclosures in the valuation report**

### *Current requirements*

- Schedule V of the InvIT Regulations prescribes the minimum set of mandatory disclosures to be made in the valuation report.

### *Proposal*

- The consultation paper proposes the following additional disclosures in the valuation report to provide investors with adequate information about the valuation and other aspects of the underlying assets of the InvITs:
  - Historical valuations made for the last three financial years for each asset, as applicable
  - Information regarding the assumed factors while calculating the valuation such as discounting rate, tenure, etc.
  - For each specific InvIT asset, certain additional details are to be disclosed such as a list of pending sanctions/approvals, periodic clearances, estimates of major repairs and improvements, ongoing litigation or tax disputes, etc.
  - Additionally, a brief summary of the valuation as per the complete valuation report should also be provided.

## Our comments

The detailed proposals in the consultation paper represent a step forward in developing a comprehensive framework for InvITs. Some of the important proposals that may require additional preparation efforts by the companies are as follows:

- Preparation of combined financial statements in accordance with Ind AS for InvITs that have been in existence for less than three complete financial years. This is a new concept and will require application of the consolidation principles to distinct assets as if these had been held by the InvIT over the past three years. SEBI has introduced this requirement based on international best practices implemented by companies for listing purposes.

Preparation of combined financial statements shall require additional efforts for compilation of relevant historical financial information based on uniform Ind AS accounting policies, alignment of reporting periods, preparation of relevant Ind AS disclosures, etc. InvITs may refer to relevant international guidance on this subject, such as that issued by the Federation of European Accountants.

- Since the financial information in the combined financial statements is required to be audited, the consultation paper requires the InvIT auditor to rely on the reports of the auditors of the financial statements of various InvIT assets. Where such historical financial statements have not been prepared in accordance with Ind AS, further information may have to be compiled by the InvIT for the InvIT auditor to perform additional procedures.
- The consultation paper also requires the audit projections of revenues and cash flows. Since this is a new requirement InvITs may need to develop and implement appropriate systems or procedures to for this.
- In addition to complying with the requirements of Ind AS 24, the consultation paper specifies minimum disclosures for related party transactions. Some of these are in addition to the Ind AS 24 requirements and may entail more detailed disclosures. InvITs would need to carefully analyse the additional requirements when preparing their financial information.

## Next steps

The consultation paper seeks public comments on the proposals suggested with the last day being 31 July 2016.



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In our recent call, on 11 July 2016, we covered the following topics:

- SEBI relaxes norms for Ind AS compliant quarterly results
- MoF defers ICDS by one year
- ITFG: Clarification Bulletin 3.

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



### Issue no. 10/2016 – Consumer Markets

This month the Accounting and Auditing Update focusses on the consumer markets sector and highlights key matters relating to accounting, financial reporting and regulatory areas relevant to this sector. The Indian Accounting Standards (Ind AS) largely converged with the International Financial Reporting Standards (IFRS) are bringing about a paradigm shift in financial reporting in India. Our article highlights two key areas of impact: revenue recognition and the consideration of embedded leases and explains the new accounting requirements in these areas and the expected challenges that are likely to be faced by the sector. The publication also features an interaction with Mr. V. Srinivasan, Chief Financial Officer and Company Secretary, Godrej Consumer Products Limited and explores some key accounting, reporting and other topical matters relevant to the industry. This publication also carries an article on fraud risk, which assesses key implications of fraud risk areas on this sector. We also seek to highlight considerations and challenges that companies in this sector could face while implementing Internal Financial Controls and key updates in the Foreign Direct Investment policy relating to this sector.

In this publication, we lay emphasis on how transfer pricing affects the sector, via complex issues relating to advertisement, marketing and promotion expenditure and an overview of the recent judgements of Indian courts in this area. We also cast our lens on distinct features and challenges associated with accounting and reporting for the liquor industry, a key sub-sector within consumer markets.



### The MCA amends certain provisions relating to auditor's rotation and managerial remuneration

8 July 2016

The Companies Act, 2013 (2013 Act) became largely effective from 1 April 2014. The Ministry of Corporate Affairs (MCA) has been issuing various amendments and clarifications to the 2013 Act and to the corresponding Rules to remove practical challenges faced by companies while implementing certain provisions of the 2013 Act. Recently, on 30 June 2016, the MCA amended certain provisions relating to:

- Auditor's rotation, and
- Companies (Appointment and Remuneration of Managerial Personnel) Rules, 2014.

Our First Notes provide an overview of the amendments made by the MCA.

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