PwC ReportingPerspectives

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Editorial

We are pleased to bring you our quarterly newsletter covering the latest developments in financial reporting as well as other regulatory updates.

All companies are required to prepare separate financial statements under Ind AS, and additionally consolidated financial statements where applicable. We have included an overview of certain important aspects specifically impacting separate financial statements under Ind AS, particularly transactions involving related entities within a group that pose unique challenges.

The Auditing and Assurance Standards Board of ICAI has recently brought out two important implementation guides on auditors' reports under Ind AS for the transition phase and audit of IFCFR with specific reference to smaller, less complex companies. The guide on the auditor's report under Ind AS provides guidance on the auditor's reporting responsibilities on financial statements prepared as per Ind AS, especially during the transition phase. On the other hand, the guide on IFCFR explains how the guidance note on the audit of IFCFR may be applied to the audits of smaller, less complex companies while also addressing some of the practical difficulties that may arise during such audits. This guide is also helpful to auditors in designing and executing the audit strategy. We discuss the key takeaways from both the guides in this edition.

ICAI formed ITFG, which issued its fourth and fifth bulletins addressing certain issues related to the applicability and implementation of Ind AS. This edition summarises the clarifications from these bulletins and also includes the FAQ issued by the Accounting Standard Board of ICAI on accounting of dividend distribution tax under Ind AS.

ICAI has also issued a guidance note on combined and carve-out financial statements which clarifies the meaning of combined/carve-out financial statements, indicative situations in which such statements may need to be prepared, procedures for preparation and required disclosures. This guidance note is particularly helpful because the accounting standards do not include specific guidance on the preparation of combined and carve-out financial statements. We have elaborated on the key requirements of this guidance note in this edition.

Finally, we have summarised other Indian as well as global regulatory updates.

We hope you find this newsletter informative and of continued interest. We welcome your feedback at *pwc.update@in.pwc.com.*

Separate financial statements

Introduction

Separate financial statements are those presented by a parent (i.e. an investor with control of a subsidiary) or an investor with joint control of, or significant influence over, an investee, in which the investments are accounted for at cost or in accordance with Ind AS 109, *Financial instruments*.

Ind AS 27, *Separate financial statements,* is the main accounting standard that deals with the preparation of separate financial statements. Separate financial statements should be prepared in accordance with all applicable Ind ASs. This includes applying the provisions of Ind AS 1, *Presentation of financial statements*, in preparing and presenting general purpose financial statements in accordance with Ind ASs, and the disclosure and measurement provisions from other Ind ASs as applicable. Specific guidance for the recognition and measurement of investments in subsidiaries, joint ventures and associates is also provided in Ind AS 27.

Scope

Ind AS 27 does not mandate which entities should produce separate financial statements. This standard shall be applied in accounting for investments in subsidiaries, joint ventures and associates when an entity elects, or is required by law, to present separate financial statements.

Recognition and measurement of investments in subsidiaries, associates and joint ventures

Investments in subsidiaries, associates and joint ventures in an entity's separate financial statements are accounted for:

- at cost, or
- in accordance with Ind AS 109

The same accounting should be applied for each category of investments. For example, an entity may adopt a policy to carry subsidiaries at cost and associates in accordance with Ind AS 109, or vice versa, in its separate financial statements. An entity may make an accounting policy choice to carry a specific category of investments at fair value in accordance with Ind AS 109. All such investments should, in principle, be measured at fair value. However, Ind AS 109 does indicate that, in very limited circumstances, cost might be an appropriate estimate of fair value. These circumstances might include, where insufficient recent information is available, or there is a wide range of estimates of fair value and cost represents the best estimate of fair value within that range. Ind AS 109 also includes a number of indicators of when cost might not be representative of fair value.

Initial recognition: Cost

Ind AS 27 does not define cost. Cost is the fair value of consideration given by the purchaser. The two commonly encountered questions in the determination of cost in separate financial statements are transaction costs and contingent consideration.

Cost is usually understood to include transaction costs. Cost generally includes the purchase price and other costs directly attributable to the acquisition or issuance of the asset, such as professional fees for legal services, transfer taxes and other transaction costs. This equally applies to investments in subsidiaries, associates and joint ventures accounted for at cost in separate financial statements.

Contingent consideration

Ind AS 27 contains no specific guidance on how to account for contingent consideration in separate financial statements. At the date of acquisition, an estimate of the contingent consideration is included as part of the cost of the acquisition. However, there may be different treatments for subsequent changes in contingent consideration. Contingent consideration is classified either as equity or as a liability/asset. If classified as equity, it is not remeasured after the acquisition date and its subsequent settlement should be accounted for within equity. In contrast, contingent consideration classified as an asset or a liability is remeasured subsequently.

The following two methods are considered acceptable accounting policy choices for subsequent changes in contingent consideration that represents a financial liability/asset:

- Subsequent remeasurement through profit and loss. If contingent consideration represents a financial liability or a financial asset, the requirements of Ind AS 109 should be followed. Ind AS 109 requires subsequent remeasurement of the financial liability/asset to be recognised in profit and loss. Such treatment would also be consistent with the treatment required by Ind AS 103, *Business Combinations* in the consolidated financial statements.
- Cost-based approach: The subsequent remeasurement of the financial liability/asset is adjusted against the cost of investment. This can be supported in an entity's separate financial statements, given that cost being the fair value of the consideration given. This is also consistent with the current practice of cost accumulation in respect of PP&E and investments in associates and joint ventures.

The acquirer should select an appropriate accounting policy and apply it consistently to all transactions.

Subsequent measurement

Investments accounted for at cost are not subsequently remeasured. Such investments are measured in the separate financial statements at the original cost of the investment until the investment is derecognised or impaired.

Step acquisitions

Where an entity increases its investment in an associate, joint venture or subsidiary which is held at cost, the carrying value will be the accumulated cost. This approach is also applied where an additional investment results in an associate/joint venture becoming a subsidiary, if both classes of investment are carried at cost.

Recognition and measurement of investments in subsidiaries, associates and joint ventures – Ind AS 109

An investor applying Ind AS 109 to its investments in a subsidiary, associate or joint venture should initially and subsequently measure those investments at fair value. An entity has the ability to make an irrevocable election on initial recognition, on an instrument-by-instrument basis, to present subsequent changes in fair value in OCI rather than profit or loss. If this election is made, all fair value changes, excluding certain dividends, will be reported in OCI. Dividends are recognised in profit and loss, unless they represent a recovery of part of the cost of an investment, in which case they are recognised in OCI.

There is no recycling of amounts from OCI to profit and loss—for example, on sale of an equity investment—nor are there any impairment requirements. However, the entity may transfer the cumulative gain or loss within equity.

Transaction costs are not included as part of the initial cost of an investment classified as 'fair value through profit or loss'.

Investments measured in accordance with Ind AS 109 are subject to the subsequent measurement guidance in that standard.

Impairment

The impairment testing of investments in subsidiaries, associates and joint ventures in separate financial statements depends on the accounting policy choices made for the measurement of such investments. Investments in subsidiaries, associates and joint ventures that are accounted for at cost in separate financial statements are within the scope of Ind AS 36 *Impairment of assets*. The accounting for investments that are accounted for in accordance with Ind AS 109 is addressed in that standard.

Ind AS 36 requires an impairment test when indicators of potential impairment exist. Indicators of potential impairment are set out in paragraph 12 of Ind AS 36. In particular, the receipt of a dividend from a subsidiary, joint venture or associate that meets the following conditions might be an internal indicator that the related investment could be impaired. The investor is, therefore, required to test the related investment for impairment where a dividend is received and:

- there is evidence available that the carrying amount of the investment in the separate financial statements exceeds the carrying amount of the investee's net assets, including associated goodwill in the consolidated financial statements; or
- the dividend exceeds the total comprehensive income of the subsidiary, joint venture or associate in the period that the dividend is declared.

When impairment indicators exist, a test for impairment should be performed. An impairment loss occurs when the carrying amount of the investment exceeds its recoverable amount. The carrying amount of an investment carried at cost would be its original cost less any previous impairment losses recognised. The recoverable amount of the investment is the higher of its fair value less costs of disposal and its value in use.

Impairment: Investment in subsidiaries

A goodwill impairment on consolidation indicates a decrease in value since acquisition. This will also trigger an impairment review of the parent entity's investment in the relevant subsidiary in the parent's separate financial statements.

The goodwill and other net assets in the consolidated financial statements that are attributable to an impaired subsidiary will usually differ from the subsidiary's carrying value in the parent's separate financial statements. The subsidiary's net assets in consolidated financial statements (including goodwill) might be lower than the amount of the parent's investment recorded at cost. This does not necessarily mean that there is an impairment loss of the investment. The carrying amount of the investment in separate financial statements should be compared with its recoverable amount (i.e. the higher of fair value less costs of disposal and value in use), rather than the carrying amount of the subsidiary's net assets.

If the recoverable amount of an investment in a subsidiary is determined by value in use, the investor's share of the present value of the subsidiary's estimated cash flows may be a proxy for value in use in separate financial statements where the parent is able to control the extraction of dividends from the subsidiary. The above is true if the subsidiary has no debt. Otherwise, the present value of expected cash flows from the subsidiaries' underlying assets should be reduced by the fair value of outstanding debt in order to determine the net amount available to equity holders. The investor's share of this net amount is the amount to use in the impairment test.

When performing an impairment review of an investment in a subsidiary, it is necessary to consider non-interest bearing inter-company balances, such as trade receivables and payables, between the parent and subsidiary. Any cash outflows payable to the parent for settlement of inter-company trading balances are included in determining the subsidiary's cash flows for use in the impairment calculation. This is because, from an entity perspective, it is expected that there will be a cash outflow from the subsidiary. Similarly, any cash inflows from the parent to the subsidiary are also taken into account. Any inter-company receivable in the parent's separate financial statements is separately evaluated based on the guidance in Ind AS 109.

Impairment: Investment in associates and joint ventures

If the recoverable amount of an investment in an associate or a joint venture is determined by value in use, the investor's share of the present value of theinvestment's estimated cash flows may be a proxy for the present value of dividend receipts. Paragraph 42 of Ind AS 28 indicates that, when appropriate assumptions are used, both methods give the same result. The appropriate assumptions to align the investment's cash flows to those of the investee will principally include reflecting the fact that the investment is a minority holding. This is typically addressed through the application of a higher discount rate to the total company cash flows, reflecting the fact that the investor does not control them or the amount which may be paid as a dividend. There might be other issues which need to be addressed, such as the impact of any restrictions on dividends and the rights of other equity holders.

Dividend income

An investor is required to recognise dividends received from a subsidiary, joint venture or associate accounted for at cost or in accordance with Ind AS 109 in its separate financial statements as income. Dividend income is within the scope of Ind AS 18 *Revenue*.

There might be situations where it is unclear whether a distribution received is a return on capital (dividend income) or a return of capital. In such cases, judgement should be applied in determining the appropriate accounting treatment, based on the substance of the transaction.

A subsidiary may decide to issue new shares to its parent for no additional consideration by capitalising reserves (as permitted by local law) into share capital. The parent makes no entries in its separate financial statements. No gain is recognised and the carrying amount of the investment in the subsidiary is not changed. No distribution is deemed to have occurred. Ind AS 27 requires the receipt of a distribution from the subsidiary in order for the parent to record income from the investment.

Disposal of investments

When an investment is either wholly or partially disposed, derecognition principles in Ind AS 109 should be applied.

Where a disposal results in the reduction of an interest in an investment held at cost which remains a subsidiary or an associate, the change in the carrying amount of the investment will be proportionate to the part disposed. Where there is a step down from subsidiary to associate, the measurement of the carrying amount of the investment in the associate depends on whether the existing accounting policy for investments in associates is at cost or at fair value in accordance with Ind AS 109. For example, if the entity has a policy of recording associates at cost, there is no clear guidance in Ind AS 27 on what cost represents. In our view, a similar proportionate approach can be applied.

First-time adoption

A first-time adopter that chooses an accounting policy of cost for its investments may recognise such investments either at cost determined in accordance with Ind AS 27 or at their deemed cost. The deemed cost is either:

- the fair value of the investment (determined in accordance with Ind AS 109) on the date of transition to Ind AS; or
- the previous GAAP carrying amount of the investment at the date of transition.

The deemed cost option is invoked separately for each investment in a subsidiary, joint venture or associate.

Certain related party transactions with entities within a group

Group share-based payment arrangements

The scope of Ind AS 102 *Share-based payment* is broad. Share-based payment transactions include transactions settled in an entity's own shares as well as transactions settled in equity instruments of the entity's parent or any other entity in the same group. So, if a subsidiary's employees are awarded options over shares of the parent, the subsidiary will recognise an expense for the employee services received.

Ind AS 102 provides a clear basis to determine the classification of awards in both consolidated and separate financial statements; it sets out the circumstances in which group share-based payment transactions are treated as equity-settled and cash-settled. The entity receiving goods or services should assess its own rights and obligations (as well as the nature of awards granted) to determine the accounting treatment. The amount recognised by the group entity receiving the goods or services will not necessarily be the same as the amount recognised in the consolidated financial statements.

Example 1 – Parent entity grants share awards to subsidiary employees

A parent grants its shares directly to the employees of subsidiaries A and B. The awards will vest immediately, and the parent will issue new shares directly to the employees. The parent will not charge subsidiaries A and B for the transaction.

In the separate financial statements of subsidiaries, the award is treated as an equity-settled share-based payment; this is because the subsidiaries do not have an obligation to settle the award. An expense for the grant date fair value of the award is recognised over the vesting period, and a credit is recognised in equity. The credit to equity is treated as a capital contribution because the parent is compensating the subsidiaries' employees with no expense to the subsidiaries. In this example, the shares vest immediately, so an expense is recognised in the subsidiaries' income statement in full (based on the grant date fair value) and there is a credit to equity.

In the separate financial statements, the parent entity records a debit, recognising an increase in the investment in the subsidiaries, and a credit to equity. This is because the employees are not providing services to the parent. These accounting entries are recognised over the award vesting period.

Example 2 – Subsidiary grants rights over parent's equity instruments

Instead of granting rights over its own equity instruments, subsidiary A grants rights over the parent's shares to its own employees. The shares vest over two years. When the shares vest, subsidiary A purchases shares from the market and passes them to its employees. Subsidiary A only makes these purchases when it settles the award with its employees.

Subsidiary A has the obligation to settle the award (albeit in the parent's shares), so Ind AS 102 requires the award to be treated in subsidiary A's financial statements as a cash-settled share-based payment because parent company shares would be an asset (not equity) in A's financial statements. An expense is recognised in the income statement over the vesting period, and a liability is recorded as the other side of the entry. This liability is remeasured at each reporting date until settlement (in accordance with the accounting for cash-settled awards).

The above transaction has no impact on the parent's financial statements; this is because the parent is not a party to the transaction.

Intra-group financial guarantee contracts

Intra-group financial guarantee contracts are not exempted from Ind AS 109's requirements and, on a stand-alone basis, will have to be measured in accordance with the standard. On a consolidation basis, the financial guarantee is not recognised as a separate contract, but is part of the group's liability to a third party (for example, a guarantee given by the parent to a subsidiary's bankers in the event the subsidiary fails to repay a loan to the bank when due). In the separate financial statements, the financial guarantee is recognised initially at fair value in accordance with Ind AS 109 (unless Ind AS 104, *Insurance contracts* applies).

Establishing such a fair value may be difficult if the financial guarantee contracts between related parties were not negotiated at arm's length and there are no comparable observable transactions with third parties. Given that intra-group guarantees are unlikely to be negotiated in a 'stand-alone arm's length transaction', fair value would have to be estimated.

As the fair value of an intra-group guarantee is unlikely to be equal to the fee charged, if any, the issuer would need to determine whether any difference should be treated as an expense or a capital contribution via an increase in investments in the subsidiary. This is an accounting policy choice. The method used should reflect the transaction's economic substance, be applied consistently to all similar transactions and be clearly disclosed in the financial statements.

Where a parent entity provides a guarantee to a bank that has advanced a loan to one of its subsidiaries, the subsidiary has obtained a benefit in that it would pay a lower rate of interest on the loan than it would have otherwise paid for an unguaranteed loan. The subsidiary could fair value the loan from the bank by reference to a normal market rate of interest it would pay on a similar but unguaranteed loan and take the benefit of the interest differential to equity as a capital contribution from the parent. Alternatively, the subsidiary could view the unit of account as being the guaranteed loan and therefore the fair value would be expected to be the face value of the proceeds the subsidiary receives. Ind AS 109 does not address the accounting for financial guarantees by the beneficiary and there is no requirement in Ind AS 24 to fair value non-arm's length related party transactions. Therefore, there is an accounting policy choice as to whether a capital contribution is recognised in equity by the subsidiary for the benefit of the lower rate of interest on the loan than it would have otherwise paid for an unguaranteed loan.

Intra-group loans

Parent entities commonly provide funding to subsidiaries; they may also provide funding to associates and joint ventures. Such funding arrangements can take many forms. At one end of the spectrum, the loan may bear a market rate of interest and be repayable at a fixed date in the future; on the other end, the loan may bear no interest and have no fixed terms for repayment—that is, no documented terms at all. In order to determine the appropriate accounting treatment for a particular loan, management needs to assess whether that loan is within the scope of Ind AS 109, or represents an interest in a subsidiary, associate or joint venture, which is outside the scope of Ind AS 109.

All financial instruments within the scope of Ind AS 109 should be recorded at fair value at the time of initial recognition. In the majority of circumstances, the fair value of a financial instrument is equal to the transaction price established between the parties to the contract, but this will not always be the case, particularly where the transaction occurs between related parties and does not bear a market rate of interest.

Interests in subsidiaries, associates and joint ventures that are accounted for under Ind AS 27/Ind AS 28, are excluded from the scope of Ind AS 109 and may be measured at cost.

The appropriate treatment for any particular transaction depends on the facts and circumstances of that transaction. Evidence of past payments or planned payments should be considered together with any contractual or agreed terms.

Loan at non-commercial rates with fixed term

Background

A parent provides a loan to a subsidiary. The loan bears no interest, but the loan agreement includes fixed terms for repayment. There are no transaction costs incurred on the issuance of the loan.

? *Question:*

How is the loan accounted for by the parent entity in its separate financial statements?

i *Response:*

The loan is initially recognised at its fair value, which in this case would be equal to the present value of the future cash to be received discounted using the prevailing market rate for a similar instrument with a similar credit rating.

As a result of the non-market interest rate inherent in the loan, there will be a difference between the cash paid and fair value on initial recognition. The parent will have to consider the economic substance of the transaction to determine whether the difference can be considered as an addition to the investment in the subsidiary.

? *Question:*

How is the loan accounted for by the subsidiary in its financial statements?

i *Response:*

The loan meets the Ind AS 32 *Financial instruments:- Presentation* definition of a financial liability. The liability is initially recognized at its fair value. In this case, it is equal to the present value of the future cash to be paid discounted using the prevailing market rate for a similar instrument with a similar credit rating. The subsidiary will have to consider the economic substance of the transaction to determine whether the difference can be considered as an addition to subsidiary's equity.

Reporting on Ind AS financial statements

Background

As we know, Ind AS has become applicable to companies in a phased manner for accounting periods beginning on or after 1 April 2016, with comparatives for 31 March 2016 or thereafter. Companies were also permitted to adopt Ind AS early on a voluntary basis for accounting periods beginning on or after 1 April 2015 with comparatives for 31 March 2015 or thereafter. A separate roadmap for banking companies, insurance companies and NBFCs has been issued in March 2016, with Ind AS becoming applicable in a phased manner for accounting periods beginning on or after 1 April 2018, with comparatives for the periods ending 31 March 2018.

In this regard, the Companies (Indian Accounting Standards) Rules, 2015, were notified by MCA on 16 February 2015. Further, for listed companies, the SEBI clarified that, while publishing its quarterly/annual financial results, companies adopting Ind AS should ensure that the comparatives filed along with such quarterly/annual financial results are also Ind AS compliant.

On transitioning to Ind AS, a company's first set of Ind AS financial statements includes:

a. three balance sheets, i.e. the opening balance sheet as at the beginning of the previous year, the comparative balance sheet as at the end of the previous year and the current year's balance sheet;

b. two statements of profit and loss, cash flow statements and statements of changes in equity for the current year and the previous year;

c. reconciliations from the previous GAAP to Ind AS in respect of equity and total comprehensive income for the previous periods.

Further, as a preparatory measure, companies may prefer preparing special purpose financial statements, for internal management purposes or otherwise, to understand the implications of the transition.

Auditing Ind AS financial statements

To help address the reporting responsibilities of auditors, the Auditing and Assurance Standards Board of the ICAI has issued the Implementation Guide on Auditor's Report under Ind AS for the transition phase (the Guide).

Three balance sheets,
i.e. the opening balance sheet as at the beginning of the previous year, the comparative balance sheet as at the end of the previous year and the current year's balance sheet

Two statements
of profit and loss, cash flow statements and statements of changes in equity for the current year and the previous year

Reconciliations
from the previous GAAP to Ind AS in respect of equity and total comprehensive income for the previous periods

Previous period figures

The Guide discusses the principles set out in SA 710 with regard to the audit under the corresponding figures approach and the comparative figures approach. In the corresponding figures approach, the auditor's opinion refers only to the current period. The previous period figures are included in the financial statements and are to be read only in relation to the amounts and other disclosures relating to the current period figures. In the comparative figures approach, the auditor's opinion refers to each period for which the financial statements are presented and an audit opinion is expressed.

The fact that Ind AS requires restating or adjusting of the opening balances in certain circumstances does not necessitate the comparative figures approach under the Indian financial reporting framework. This is in view of paragraph 6 of the 'General Instructions for the Preparation of Financial Statements of a Company Required to Comply with Ind AS' in Schedule III to the Companies Act, 2013, which requires the financial statements to contain the corresponding amounts for the immediately preceding reporting period. The audit of the Ind AS financial statements/ results therefore, would follow the corresponding figures approach. Further, as per the SA 710 and SA 510, 'Initial Audit Engagements – Opening Balances', the current auditor can rely on the comparative information audited by the predecessor auditor.

Responsibility for the opening balance sheet/ corresponding figures

The accounting requirements to be followed with regard to the opening balance sheet is set out in Ind AS 101 and require companies to apply the same Ind AS compliant accounting policies in its opening balance sheet and throughout all periods presented in its first complete set of Ind AS financial statements. Where the previous period's financial statements were audited by a predecessor auditor, there could be two scenarios:

a. the incoming auditor audits the corresponding figures for adjustments to transition to Ind AS by placing reliance on the predecessor auditor's opinion as envisaged in SA 710;

b. the predecessor auditor audits the adjustments to the corresponding figures for transition to Ind AS and gives an audit opinion on the same. The incoming auditor may rely on the audit of the predecessor auditor; however, he should also comply with SA 710 and SA 510.

Under scenario (a), where the incoming auditor audits the adjustments for transition to Ind AS while relying on the audit under the previous GAAP by the predecessor auditor, he includes an 'Other Matter' paragraph in his audit report to highlight the fact of reliance on the work of the predecessor auditor under previous GAAP for corresponding figures and that he has performed audit procedures on the adjustments to such corresponding figures as required by applicable Ind AS.

Under scenario (b), where the predecessor auditor audits the transition adjustments, such audit would be carried out under SA 800 and his audit report will be forwarded by the company to the incoming auditor for consideration. In this case, the incoming auditor suitably discloses this fact as an Other Matter paragraph in his audit report.

Reporting on the Ind AS financial statements for the corresponding period and opening Ind AS balance sheet

In instances where the company gets the comparative Ind AS financial statements audited in advance of preparing its first complete set of Ind AS financial statements, the auditor (predecessor or incoming) is required to issue a separate report on such financial statements. In such instances, the notes to the financial statements should describe that, as part of conversion, the company has prepared its comparative Ind AS financial statements necessary for providing the information expected to be included in the company's first complete set of Ind AS financial statements, and the comparative information is not included.

In this regard, the audit report should:

a. Follow the requirements of SA 800. In case of a time lag for the regulatory requirement for presentation of the first complete set of Ind AS financial statements, there may be significant uncertainty on the accounting policies that will be followed. Hence, an Emphasis of Matter paragraph should be included to explain that the Ind AS accounting policies applied in preparing these financial statements may be subject to change.

b. Have an appropriate title, e.g. 'special purpose independent auditor's report on the preliminary comparative Ind AS financial statements'.

c. Include emphasis of matter paragraphs to highlight that the financial statements were prepared to provide corresponding figures expected to be included in the company's first complete set of Ind AS financial statements and that comparative information for the previous year has not been included.

The special purpose comparative Ind AS financial statements, if issued, cannot be referred to as audited unless the auditor's report is also attached or is available in the public domain.

Review/audit of quarterly/annual Ind AS financial results under SEBI Regulations

To comply with SEBI Regulations for Ind AS compliant corresponding figures, suitable adjustments would be required to be made to corresponding figures prepared as per previous GAAP to bring them in conformity with Ind AS. SEBI has presently relaxed the requirement for presenting comparative information. However, where the company opts to present figures for the corresponding periods, the principles stated in the previous paragraphs would apply.

Others

The Guide deals with the auditor's responsibility in special situations, such as filing of offer documents with SEBI and reference to the auditor's expert in the auditor's report. Formats for the independent auditor's reports on the standalone Ind AS financial statements, the comparative Ind AS financial statements and for listed companies, the limited review/audit report on the financial results are also provided. These formats would need to be appropriately modified when SA 701, relating to key audit matters, becomes applicable.

In conclusion

The Guide provides much-needed guidance to auditors in reporting on a company's first Ind AS financial statements. The formats contained in the Guide provide insights to companies and investors on the auditor's considerations in reporting. Upfront two-way communication between auditors and preparers of Ind financial statements would ensure value to the stakeholders by way of optimum disclosures in the financial statements and appropriate disclosures in the auditor's report.

Audit of internal financial control over financial reporting for smaller, less complex companies

Pursuant to the requirement of section 143(3)(i) of the Companies Act, 2013, auditors of all companies are required to report on whether the company has adequate internal financial controls and that they are operating effectively.

To address some of the specific concerns raised by the members with respect to the audit of IFCFR of smaller and less complex entities, the Auditing and Assurance Standard Board of the ICAI has issued an Implementation Guide on Audit of Internal Financial Controls over Financial Reporting with Specific Reference to Smaller, Less Complex Companies (the Implementation Guide) which should be read in conjunction with the Guidance Note on Audit of Internal Financial Controls over Financial Reporting (the Guidance Note) while carrying out the audits of IFCFR in case of smaller, less complex companies.

This Implementation Guide discusses how the guidance given in the Guidance Note may be applied to the audits of IFCFR in the case of smaller, less complex companies and addresses some of the practical difficulties that may arise during the audits. The Implementation Guide is also helpful to the auditors to design and execute the audit strategy.

The Implementation Guide is divided into specific sections:

(1) Understanding and scoping,
(2) considerations of certain characteristics
(3) reporting considerations.

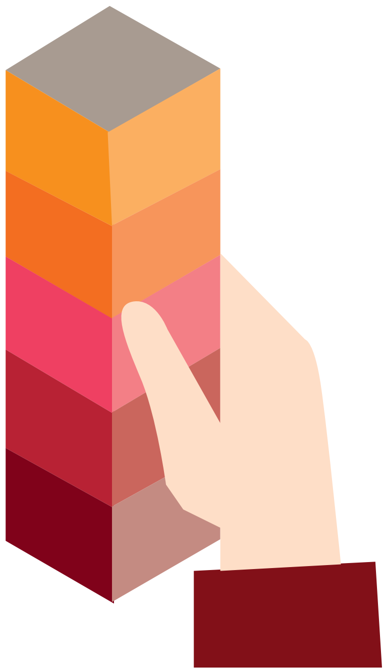
It also includes appendices containing illustrations of controls and auditor's reports. Relevant highlights from the Implementation Guide are as under:

The Implementation Guide clarifies that smaller is a relative term covering a wide range of companies that may possess some or similar characteristics. Factors that may indicate less complex operations include concentration of ownership and management by a small number of individuals; straightforward or uncomplicated transactions; simple record-keeping/ centralised accounting; few lines of business and few products within business lines; few personnel, many having a wide range of duties; use of less complex IT systems.

The Implementation Guide identifies some of the areas where the IFCFR audit of a smaller, less complex company may require special consideration considering the nature of business, size of operation and organisational structure, and this includes:

- Obtaining sufficient appropriate audit evidence for companies having limited/less formal documentation;
- Assessing entity-level controls to sufficiently address risks of misstatement;
- Evaluating the 'risk of management override' and its mitigating actions;
- Evaluating controls implemented in lieu of segregation of duties;
- Evaluating financial reporting competencies.

In respect of materiality and risk assessment for an IFCFR audit, the Implementation Guide states that the auditor should use the same materiality considerations used in planning the audit of the company's annual financial statements as provided in SA 320, 'Materiality in Planning and Performing an Audit'. Additionally, the risk factors considered for the identification of significant accounts and disclosures and their relevant assertions in the IFCFR audit are the same as those in the audit of the financial statements. Accordingly, significant accounts and disclosures and their relevant assertions are the same for both audits.



It also acknowledges that the audit of IFCFR should be combined with the audit of the financial statements. This means that the auditor should plan and perform the work to achieve the objectives of both audits, which are as follows:

Audit of the financial statements	To express an opinion on the fairness with which the financial statements present, in all material respects, financial position, results of operations, and its cash flows in conformity with the financial reporting framework.
Audit of IFCFR	To express an opinion on the effectiveness of the company's internal control over financial reporting.

The Implementation Guide attempts to answer the most challenging issue faced by the auditors while auditing IFCFR of smaller less complex entities, i.e. the issue of not having formal documentation of the entity's processes and controls. The Implementation Guide states that if the company does not have formal documentation of its processes and controls, the auditor may consider whether other related documentation is available for obtaining sufficient understanding. A practical way to identify such other documentation is to look for the information that the company uses to run its business. Thus, it acknowledges that the absence of documentation evidencing the operation of a control does not by itself create the presumption of ineffectiveness of the control. Rather, the auditor must be satisfied that the control actually operated through other corroborating evidence that is sufficiently persuasive. The Implementation Guide clarifies that based on the assessment of evidence collectively, considering circumstances, including the nature, size and complexity of the company, the auditor in judgement may be able to conclude that the control actually operated.

On the reporting front, members raised concerns on advocating two separate audit reports, i.e. one on the audit of financial statements and the second on the audit of IFCFR. The Implementation Guide clarifies that the auditor can issue a single audit report for both financial statements and IFCFR under section 143(3) of the Companies Act, 2013, and provides an illustrative formats of the audit reports.

Similar to what has been highlighted above, the Implementation Guide includes responses to other practical difficulties and can be used by the auditors as a practice aid for carrying out an effective audit of IFCFR for smaller, less complex companies.

Clarifications from Ind AS Transition Facilitation Group and FAQ issued by Accounting Standard Board

Background

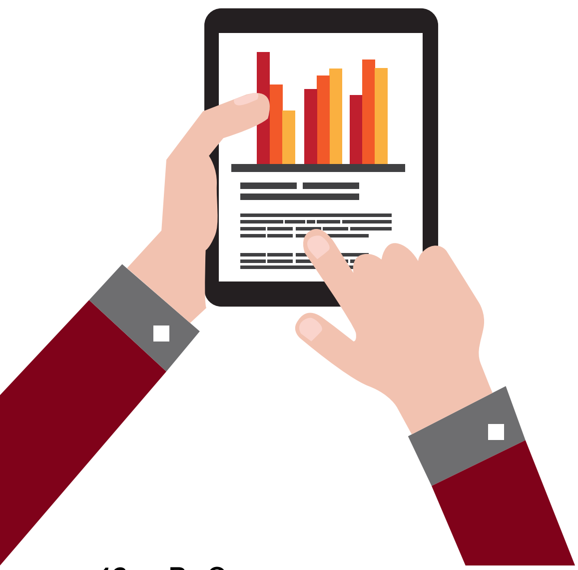
ITFG has been constituted for providing clarifications on a timely basis on various issues related to the applicability and/or implementation of Ind AS under the Companies (Indian Accounting Standards) Rules, 2015, raised by preparers, users and other stakeholders.

This article summarises the clarifications issued by ITFG in its 4th and 5th bulletins and the FAQs issued by the ASB.

ITFG Clarifications

Applicability of Ind AS

- Ind AS will be applicable to companies (both listed and unlisted) from FY 2016–17, if their net worth is 500 crore INR or more. Therefore, if the net worth of the listed or unlisted company is negative, then Ind AS will not be applicable from FY 2016-17. However, Ind AS shall be applicable to all the listed companies from FY 2017–18 irrespective of the net worth.



First-time adoption: PP&E

- If a first-time adopter chooses to continue with the carrying value of all of its PP&E as at the date of transition measured as per the previous GAAP and use that as its deemed cost at the date of transition, then the option of applying this on selective basis to some of the items of PP&E and using fair value for others is not available.
- If a first-time adopter chooses to continue with the carrying value of all of its PP&E as at the date of transition measured as per the previous GAAP and use that as its deemed cost at the date of transition, then no further adjustments to the deemed cost of PP&E shall be made for transition adjustments that might arise from the application of other Ind ASs. Accordingly, processing fees on the loan which were capitalised as part of the relevant fixed assets under previous GAAP shall remain capitalised as part of the deemed cost of PP&E. The adjustment related to the outstanding loans to bring these in conformity with Ind AS 109 shall be recognised in the retained earnings on the date of transition.
- Government grants which were deducted from the carrying amount of fixed assets under previous GAAP shall not be added back to the carrying amount of fixed assets in case entities elect to continue the carrying amount of PP&E as per previous GAAP on the date of transition to Ind AS. The adjustment related to the government grant should be recognised retrospectively as deferred income with corresponding adjustments in the retained earnings on the date of transition.
- A first-time adopter has to apply Ind AS 16 retrospectively for spare parts which were recorded as inventory under previous GAAP regardless of the fact that the entity has elected to continue with the carrying value of all of its PP&E as at the date of transition measured as per previous GAAP and use that as its deemed cost at the date of transition.
- Spare parts are generally available for use from the date of their purchase. Accordingly, spare parts recognised as PP&E shall be depreciated when the same are available for use.

Others

- Entities are required to evaluate the lease agreement to ascertain the real intention and attributes of escalation in lease payments, i.e. whether the intention of such escalation is to compensate for expected general inflation or any other factors to determine whether lease payments shall be recognised as an expense on a straight-line basis or not. It is not necessary that the rate of escalation of lease payments be exactly equal to the expected general inflation. If the actual increase or decrease in the rate of escalation is not materially different as compared to the expected rate of inflation under the lease agreement, it is not required to straight-line the lease payments. However, the purpose of such escalation should only be to compensate the expected general inflation rate. For example, where the lease escalation rate is 15% per annum and general inflation rate in the country for the lease period is expected to be 6%, then in such situations the entire lease payments should be straight-lined because the increase of 15% per annum does not appear to have any link with the general inflation which is expected to be 6%.
- The accounting of return of investment in a joint venture LLP in the separate financial statements of investor shall depend on the terms of the contract between investor and LLP. The share of profit in LLP shall be recognised as income in the statement of profit and loss as and when the right to receive its profit share is established.
- An electricity company shall classify the security deposits which are refundable when the connection is surrendered by customers as current liability. Although it is expected that most of the customers will not surrender their connection and the deposit need not to be refunded, surrendering of the connection is a condition that is not within the control of the entity. Hence, the electricity company does not have a right to defer the refund of deposit. The expectation of the company that it will not be settled within 12 months is not relevant to classify the liability as a non-current liability.
- Service tax collected represents the amount collected on behalf of a third party, viz. the government. Therefore, revenue should be net of service tax collected.
- Excise duty is a liability of the manufacturer which forms part of the cost of production, irrespective of whether or not the goods are sold. Therefore, recovery of excise duty flows to the entity on its own account and the same should be included in the amount of revenue. Since the revenue is the gross amount including excise duty, in the statement of profit and loss prepared under Ind AS, the excise duty should be reflected as an expense.
- A company covered under Phase I is required to mandatorily adopt Ind AS from 1 April 2016, i.e. for the period 2016–17 and with comparatives as per Ind AS for 2015–16. Accordingly, the beginning of the comparative period will be 1 April 2015, which will be considered as the date of transition as per Ind AS. The company cannot have the date of transition at 1 April 2014 and accordingly cannot present additional comparatives for 2014–15.

ASB- FAQ

Dividend Distribution Tax (DDT)

The presentation of DDT paid on the dividends should be consistent with the presentation of the transaction that creates those income tax consequences. Therefore, DDT should be charged to profit or loss if the dividend itself is charged to profit or loss. If the dividend is recognised in equity, the presentation of DDT should be consistent with the presentation of the dividend, i.e., to be recognised in equity. Accordingly, in case of combined financial instruments, bifurcated into debt and equity, the portion of DDT related to dividend/interest to the debt component should be recognised in profit or loss and that related to equity component should be recognised in equity.

Conclusion

ITFG and ASB have attempted to clarify certain issues related to the implementation of Ind AS. These clarifications would be helpful for companies and auditors as they navigate through Ind AS.

Guidance note on combined and carve-out financial statements

Introduction

There may be occasions such as takeovers of entities and/or divisions/segments/businesses, demergers, spin-offs and initial public offerings where specific financial information is required for part or parts of entities which may or may not be part of a group. Similarly, group financials may be required for group loan arrangements. The term 'group', in such cases, for the purpose of this Guidance Note, may include the entities and/or divisions/segments/businesses which are being combined as per the terms of the loan arrangement. In the absence of control, preparation of consolidated financial statements would not be appropriate. *In such cases, combined financial statements may be prepared* for part or parts of one or more entities. In certain circumstances, carve-out financial statements provide additional financial information for a part of an entity, such as in the case of demerger, spin-off, etc.

The combined/carve-out financial statements can include financial information pertaining to different entities, divisions, branches and/or an aggregation of similar assets, associated liabilities and operations in a specified geographic region or line of business pertaining to different entities. These financial statements can be prepared by aggregating financial statements of segments, separate entities or components of groups which may not necessarily have separate management and accounting records.

Combining businesses for which combined financial statements are prepared are generally under the common control of an entity, or a person; or the management; or they might be undertaking some common business. However, combined financial statements for combining businesses can also be prepared in other situations apart from these circumstances.

Objective

- Provides the meaning of combined/carve-out financial statements.
- Provides indicative situations in which these may be required to be prepared.
- Procedure for preparation of the same and required disclosures.

Scope

This Guidance Note applies in the preparation and presentation of combined/carve-out financial statements.

It should not be construed to be applicable to the general purpose financial statements as the combined/carve-out financial statements are prepared for specific purposes and, therefore, are 'special purpose financial statements'.

Definitions

Term	Meaning
Carve-out business	For the purpose of this Guidance Note and notwithstanding the definition of 'business' as contained in Ind AS 103, Business combinations, the term 'carve-out business' refers to an identifiable set of assets and liabilities pertaining to an economic activity carved out of the aggregate activities of an entity. A division, segment or business activity of an entity may also signify a carve-out business.
Carve-out financial statements	The financial statements pertaining to a carve-out business.
Combined financial statements	The financial statements that present the combined historical financial information of combining businesses that do not comprise a group for which the consolidated financial statements can be prepared.
Combining businesses	For the purpose of this Guidance Note and notwithstanding the definition of 'business' as contained in Ind AS 103, Business combinations, the term 'combining businesses' refers to two or more entities and/or divisions/segments/businesses of the same or different entities, historical financial information in respect of which are being aggregated for the purpose of preparation of combined financial statements.
Common control	Combining businesses are said to be under common control when all the combining entities are ultimately controlled by the same party or parties and that control is not transitory.
Financial statements	For the purpose of this Guidance Note, combined/carve-out financial statements are the complete set of financial statements that are required to be prepared by the applicable accounting standards.
Remaining group	Entities or part of entities other than the carve-out business in respect of which carve-out financial statements are prepared.

Circumstances in which combined/carve-out financial statements may be prepared

Type of financial statements	Circumstances in which these financial statements may be prepared	Examples
Combined financial statements	Combined financial statements can be prepared in cases where: a. two or more entities are combined in their entirety; or b. two or more carve-out businesses of the same or different entities are combined; or c. one or more entities are combined with one or more carve-out businesses.	a. Transactions such as acquisition or disposition negotiations/ agreement; for instance, a group of entities which do not form a group from a legal point of view, but are the subject matter of an acquisition or disposal. b. Filings in accordance with statutory or regulatory requirements, e.g. initial public offerings by real estate investment trusts, infrastructure investment trusts. c. Circumstances in which combined financial statements of commonly controlled entities are likely to be more meaningful than their separate financial statements. For example, combined financial statements would be useful if one or more individuals control several entities that are related/unrelated in their operations. d. Where two or more companies under the same group are required to prepare combined financial statements for the purpose of borrowings from banks or other financial institutions, e.g. common loan arrangements.
Carve-out financial statements	Carve-out financial statements may be prepared for one or more divisions, segments, businesses, etc., of the same entity.	Demerger, spin-off, hiving off or any other related restructuring of a segment/divisions/business of the same entity or acquisition of a segment/division/business of another entity.

Preparation of combined financial statements

Situation	Principles	Example
Preparation of combined financial statements for two or more entities	• The procedure is the same as that for consolidated financial statements. • Intra-group transactions and profits or losses should be eliminated. • Non-controlling interests, foreign operations, different financial reporting periods, accounting policies or income taxes should be treated in the same manner as in consolidated financial statements prepared under the applicable accounting standards. • In case the combining entities or any one of the combining entities are under common control, the carrying amounts pertaining to a subsidiary, as reflected in the consolidated financial statements of the parent, should be used for the purpose of preparing combined financial statements.	A Ltd. has three subsidiaries, viz. X Ltd., Y Ltd. and Z Ltd. X Ltd. has better creditworthiness and approaches the bank for a loan which will be used by both X Ltd. and Y Ltd. The bank requires combined financial statements of X Ltd. and Y Ltd. to be prepared for loan appraisal purposes. The combined financial statements of X Ltd. and Y Ltd. should be prepared using the amounts contained in A Ltd.'s consolidated financial statements pertaining to subsidiaries X Ltd. and Y Ltd.
Preparation of combined financial statements where at least one of the combining businesses is a carve-out business	• Financial statements prepared in such situations are combined financial statements irrespective of the fact that they involve one or more carve-out businesses as the combining businesses. • Follow the procedure for preparation of carve-out financial statements for the carve-out business. • Aggregate historical financial information of two or more carve-out businesses of the same or different entities; or one or more entities with one or more carve-out businesses. See the examples in the next column.	• A toll road project of company A Ltd. having various other projects is sought to be combined with a toll road project of Company B; each of the companies has remaining projects which continue to operate independently. • A toll road project of company A Ltd. having various other projects is sought to be combined with a windmill project of the same company; remaining projects continue to operate independently. • X Ltd., which is a subsidiary of A Ltd., is sought to be combined with a toll road project of A Ltd.; remaining projects of A Ltd. continue to operate independently. • X Ltd., which is a subsidiary of A Ltd., is sought to be combined with the toll road projects of A Ltd. and B Ltd.; remaining projects of A Ltd. and B Ltd. continue to operate independently.

Preparation of carve-out financial statements

1. Basis for allocating transaction amounts and balances

Where the information with regard to carve-out business is required, carve-out financial statements may have to be prepared. For preparing carve-out financial statements, difficulties in allocation may arise—e.g. payroll accounting, where a group of employees provides services for a particular carve-out business as well as for the remaining group—for instance, centralised purchasing, marketing, rent, advertising, legal, insurance and management expenses. Where transactions or balances are not directly identifiable to the carve-out assets and liabilities and income and expenses pertaining to the concerned projects (collectively termed as 'carve-out business'), it will be desirable to develop methods for allocating the relevant amounts to the carve-out business with a view to providing the fairest approximation to the amounts actually attributable to the carve-out business. An appropriate method can be adopted and applied for allocation purposes along with a disclosure of the basis adopted for allocation.

Example

Allocation of brand cost amongst various segments when only one segment is being carved out while other segments also use the brand. In such a case, brand cost may be allocated on an appropriate basis with disclosure of the basis adopted for allocation.

The appropriate basis for allocating common income and expenditure to a carve-out business will vary according to the circumstances.

Type of assets, liabilities, income and expenses	Basis of allocation
Centrally accounted for salaries and other related costs, including retirement benefits	Headcount; however, relative levels of staff turnover or other factors also need consideration.
Costs of a head office accounts department	Relevant sizes of the carve-out business and remaining group and where other factors suggest that size is not a good basis—for example, a disproportionate number of the accounting team is engaged in work for one part of the business and not the other—any other basis might be considered appropriate for the purpose of allocation.
Assets	On the basis of control, usage, legal ownership or any other appropriate basis.
Group third party debt	Debt may be treated as part of the carve-out business where it can be related to that business. In other cases, allocation may be made by reference to the terms of the separation agreement.
Finance lease liabilities	In line with the allocation of the related assets.
Interest income and expenses	In line with the allocation of related instruments.

The purpose of the allocation is to attribute an appropriate element to the carve-out business and not to measure and recognise income and expenses or assets and liabilities as if the carve-out business had always been a stand-alone entity. Thus, the resulting financial position may not be that which might have existed if the carve-out business had been a stand-alone business.

2. **Relationship with the remaining group**

- Sales which were previously regarded as 'intra-group' will need to be re-examined to determine whether they relate to entities within the carve-out business or outside it.
- Balances of a trading nature with the remaining group will normally be presented as an element of debtors or creditors.
- Balances which are considered to be funding in nature (having regard, inter alia, to the use of the funds, the period for which they remain outstanding and the level of other funds) will normally be classified according to their general nature.
  - Where the balance is interest bearing and/or has other characteristics of debt, it will be presented as debt financing.
  - Where the balance does not have the characteristics of debt, it will be classified as capital and presented as a part of equity aggregated with the owners' contribution (capital) and reserves of the carve-out business.

Example

Carve-out business was charged royalty on a periodic basis for the use of a product pertaining to an entity. From the perspective of carve-out financial statements, this fee stands payable to the owners since it is owed to the owners. It will be presented in the manner of debt financing in the carve-out financial statements since royalty is charged on a periodic basis and bears the characteristics of debt. However, in case no royalty is charged for the use of the product, then it will be treated as the owner's contribution.

- Balances with the remaining group may also contain elements of third-party debtors or creditors which have been accounted for on behalf of the carve-out business by the remaining group.

Example

VAT, payroll taxes, certain customers or suppliers common to the carve-out business and the remaining group, and external funding balances.

Such elements of the balances with the remaining group should be allocated appropriately.

3. **Exceptional items**

   Exceptional items should be allocated to the carve-out business and accounted for in accordance with the applicable accounting standards.

Aspects common to combined/carve-out financial statements

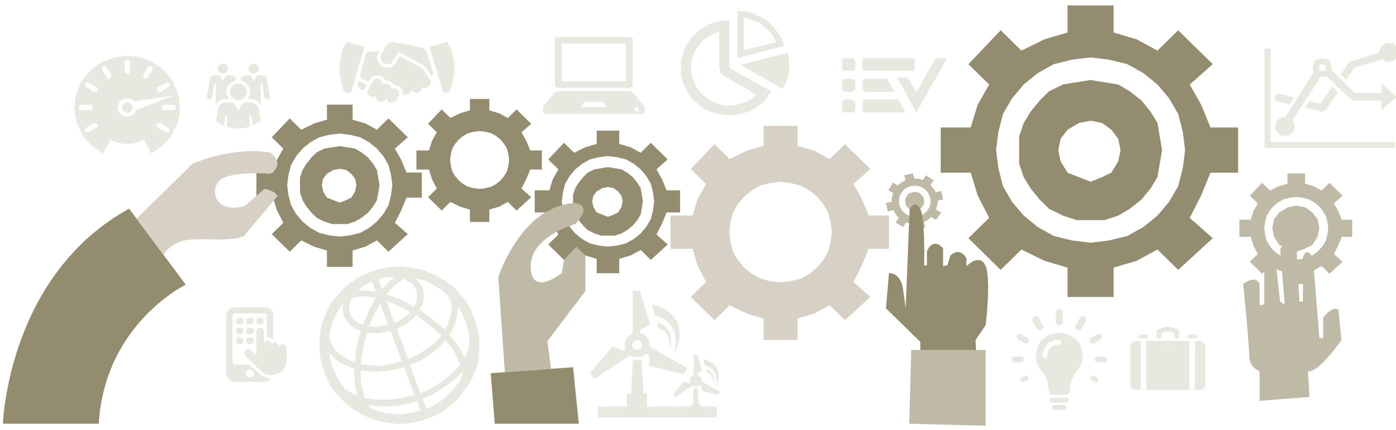
Area	Principles
Taxation	• The determination of tax expenses depends on whether the combining/carve-out businesses have filed separate tax returns or have their tax affairs dealt with as part of a larger tax entity. • Generally, tax expenses should be determined for a combining/carve-out business as if the combining/carve-out business is a separate taxable entity. • Where separate tax returns do not exist, a basis for allocating overall tax expenses must be determined on appropriate basis.
Impairment	• For each period covered by the combined/carve-out financial statements, an independent assessment of the presence or absence of impairment indicators should be made based on the position post combination. • Other provisions relating to measurement, recognition and disclosure of impairment should be governed by the applicable accounting standards.

Area	Principles
Transaction costs	• Transaction costs include finder's fees; advisory, legal, accounting, valuation and other professional or consulting fees; general administrative costs, including the costs of maintaining an internal acquisitions department; and costs of registering and issuing debt and equity securities. Such costs should be recognised as expenses in the periods in which the costs are incurred and the services are received. • The costs to issue debt or equity securities should be recognised in accordance with the applicable accounting standards.
Capital	• Where there is legal capital, the same should be considered in preparing combined/carve-out financial statements. • However, it may not be possible to arrive at the amount of share capital pertaining to combining/carve-out businesses. In such cases, the difference between the assets and liabilities of the combining/carve-out businesses, being net asset value, may be presented as capital. While doing so, to the extent balances (not having the characteristics of debt) treated as part of equity should be considered as a component of the equity.
Cash flow statements	• Prepared in accordance with the applicable accounting standards.

Disclosures

- Disclosure is required in the notes to the combined/carve-out financial statements of the fact that the information presented may not be representative of the position which may prevail after the transaction.
- Similarly, the fact that the resulting financial position may not be that which might have existed if the carve-out business/combining businesses had been a stand-alone business should also be disclosed.
- Comparatives are not necessarily required to be given for the combined/carve-out financial statements.
- Other disclosures:
  - the purpose of preparation of combined/carve-out financial statements;
  - a list of combining businesses together with brief description of activities;
  - statement of compliance with the applicable accounting standards;
  - the principal accounting policies followed in preparing the combined/carve-out financial statements;
  - the basis for allocation, critical assumptions, judgments and estimates involved in the preparation of combined/carve-out financial statements;
  - other disclosures as per the requirements of applicable accounting standards to the extent relevant;
  - where the accounting policies are not uniform in respect of the combining businesses, disclosure of that fact along with the accounting framework followed;
  - extent of balances (not having the characteristics of debt) treated as part of equity;
  - the basis of pricing inter-group transfers and any change therein.

The above disclosures are not exhaustive and specific disclosures that will assist users' understanding of combined/carve-out financial statements should also be made.



Recent technical updates

MCA

The Companies (Accounts) Amendment Rules, 2016

MCA has issued Companies (Accounts) Amendment Rules, 2016. Among other matters, the amended rules have substituted the second proviso of rule 6 of the Companies (Accounts) Rules, 2014, relating to the preparation of a consolidated financial statement by an intermediate wholly owned subsidiary with the following:

Provided further that nothing in this rule shall apply in respect of preparation of consolidated financial statements by a company if it meets the following conditions:

i. it is a wholly owned subsidiary, or is a partially owned subsidiary of another company and all its other members, including those not otherwise entitled to vote, having been intimated in writing and for which the proof of delivery of such intimation is available with the company, do not object to the company not presenting consolidated financial statements;

ii. it is a company whose securities are not listed or are not in the process of listing on any stock exchange, whether in India or outside India; and

iii. its ultimate or any intermediate holding company files consolidated financial statements with the Registrar which are in compliance with the applicable accounting standards.

Amendment to Schedule V to the Companies Act, 2013

MCA notified amendments to Section II of Part II of the Schedule V of the Companies Act; 2013. The key amendments are as follows:

i. The remuneration limits for the companies having inadequate/no profit to pay remuneration to the managerial personnel without central government approval have been amended.

ii. A new provision has been incorporated for the managerial personnel functioning in a professional capacity.

Companies (Share Capital and Debentures) Third Amendment Rules, 2016

MCA has issued Companies (Share Capital and Debentures) Third Amendment Rules, 2016. Among other matters, the amendment allows a company to issue equity shares with differential rights upon expiry of five years from the end of the financial year when the default was made good. It also requires companies which intend to redeem debentures prematurely to transfer the amount to a debenture redemption reserve as is necessary for redemption of such debentures.

Companies (Share Capital and Debentures) Fourth Amendment Rules, 2016

MCA has issued Companies (Share Capital and Debentures) Fourth Amendment Rules, 2016. According to the amendment, Rule 18 of Companies (Share Capital and Debentures) Rules, 2014, —on the conditions to be satisfied to issue secured debentures, —will not apply to rupee denominated bonds issued exclusively to overseas investors.

Companies (Cost Records and Audit) Amendment Rules, 2016

MCA has issued Companies (Cost Records and Audit) Amendment Rules, 2016. Among other matters, the rules have amended the definition of cost audit report the provisions related to the applicability of the Companies (Cost Records and Audit) Rules, 2014, and the appointment of cost auditor.

Companies (Mediation and Conciliation) Rules, 2016

The central government, in order to facilitate a voluntary dispute resolution mechanism, has issued the Companies (Mediation and Conciliation) Rules, 2016. The rules pertain to section 442 of the Companies Act, 2013, which provides for the setting up of a Mediation and Conciliation panel for facilitating mediation and reconciliation between the parties during any stage of the proceeding before the quasi-judicial bodies, i.e. the central government, Tribunal or Appellate Tribunal.

Companies (Acceptance of Deposits) Amendment Rules, 2016

MCA has issued the Companies (Acceptance of Deposits) Amendment Rules, 2016. Among other matters, it includes following amendments:

- Deposit does not include an advance towards consideration for providing future services in the form of a warranty or maintenance contract as per a written agreement or arrangement if the period for providing such services does not exceed the period prevalent as per common business practice or five years from the date of acceptance of such service, whichever is less.
- Companies may accept deposits without a deposit insurance contract till 31 March 2017 or till the availability of a deposit insurance, whichever is earlier.
- Every company other than a private company shall disclose in its financial statement by way of notes the money received from the directors and every private company shall disclose in its financial statement, by way of notes, the money received from directors or relatives of directors.

Companies Third (Removal of Difficulty) Order, 2016

MCA has issued Companies Third (Removal of Difficulty) Order, 2016, regarding the applicability of the provisions of rotation of auditors. The existing third proviso to section 139 (2) of the Companies Act, 2013 (the 'Act'), provided that every company, existing on or before the commencement of this Act, which is required to comply with the provisions of this section shall comply with such requirements within three years from the date of commencement of the said Act. The same has been substituted as follows:

'Provided also that every company, existing on or before the commencement of this Act which is required to comply with the provisions of this sub-section, shall comply with requirements of this sub-section within a period which shall not be later than the date of the first AGM of the company held, within the period specified under sub-section (1) of section 96 of the Act, after three years from the date of commencement of this Act.' This amendment shall be deemed to have come into force from 1 April 2014.

SEBI

Revised formats for financial results and implementation of Ind AS by listed entities which have listed their debt securities and/or non-cumulative redeemable preference shares

SEBI has issued a circular dated 10 August 2016 on the above-mentioned subject matter. To facilitate a smooth transition during the first year of Ind AS implementation, the circular gives various relaxations to the listed entities which have listed their debt securities and/or non-cumulative redeemable preference shares relating to timelines, format and presentation of comparatives, audit/limited review of comparative figures and format for financial results to be published in newspapers, etc.

Clarification by SEBI regarding revenue recognition and excise duty

SEBI had issued a circular dated 30 November 2015 wherein it was prescribed that 'revenue from operations' may be disclosed net of excise duty. Subsequently, Schedule III of the Companies Act, 2013, required disclosure of which was notified on 6 April 2016, required disclosure of revenue from sale of products inclusive of excise duty.

SEBI issued a circular dated 5 July 2016 wherein it was clarified that in case of any technical difficulty in the interpretation of any specific item in the formats or implementation of this circular while publishing the financial results, the listed entities shall be guided by the relevant provisions of the Ind AS Rules/AS Rules and Schedule III to the Companies Act, 2013, and may make suitable modifications, as applicable.

However, SEBI observed that some companies have been disclosing 'revenue from operations' including excise duty, and some companies have been disclosing 'revenue from operations' excluding excise duty in their financial results for the quarter ended 30 June 2016.

In order to have a uniform approach with respect to disclosure of 'revenue from operations', SEBI has issued the following clarification:

'Income from Operations', as mentioned in the formats for publishing financial results prescribed in the circular dated November 30, 2015, may be disclosed inclusive of excise duty, instead of net of excise duty, as specified in the Companies Act, 2013.

Consolidated Account Statement: Mutual Funds (Circular dated 20 September 2016)

SEBI has partially modified the requirements in the Consolidated Account Statement (CAS) issued to investors in accordance with Regulation 36(4) of SEBI (Mutual Funds)

Regulations, 1996, and circulars thereof, which provide information in terms of name of scheme(s) where the investor has invested, number of units held and their market value, among other details.

Consultation paper for amendments to SEBI (Real Estate Investment Trusts) Regulations, 2014

To solicit comments/views from the public on suggestions pertaining to making amendments/providing clarifications to SEBI (Real Estate Investment Trusts) Regulations, 2014 (hereinafter referred as 'REIT Regulations'), certain amendments/clarifications are proposed for REIT Regulations. Proposal for consultation includes:

- Clarifying the definition of 'associates' in the regulations.
- Clarifying the definition of 'real estate property' in the regulations.
- Increasing the number of sponsors.
- Rationalising compliance with respect to related party transactions requirements.
- Aligning minimum public holding requirement with the Securities Contracts (Regulation) Rules, 1957.
- Allowing REITs to invest up to 20% in under construction assets.
- Assigning responsibilities to a trustee and its associates.
- Managing operational aspects.
- Removing the restriction on an SPV (only in case such SPV being a holding company) investing in other SPVs holding the assets.

RBI

Applicability of Ind AS to AIFIs

RBI vide circular dated 4 August 2016 has advised that select AIFIs (Exim Bank, NABARD, NHB and SIDBI) shall follow Ind ASs as notified under the Companies (Indian Accounting Standards) Rules, 2015, subject to any guideline or direction issued by the RBI in this regard, in the following manner:

i. AIFIs shall comply with Ind ASs for financial statements for accounting periods beginning from 1 April 2018 onwards, with comparatives for the periods ending 31 March 2018 or thereafter. Ind AS shall be applicable to both stand-alone financial statements and consolidated financial statements. 'Comparatives' shall mean comparative figures for the preceding accounting period.

ii. AIFIs shall apply Ind AS only as per the above timelines and shall not be permitted to adopt Ind AS earlier.

AIFIs also need to be in preparedness to submit proforma Ind AS financial statements as per the formats given in Annexures I to IV of the circular and the associated guidance given in Annexure V of the circular to the RBI from the half-year ended 30 September 2016 onwards. The proforma statements for the half year ended 30 September 2016 shall be submitted latest by 30 November 2016.

Prudential Norms for Off-balance Sheet Exposures of Banks: Restructuring of derivative contracts

The circular on Prudential Norms for Off-balance Sheet Exposures of Banks requires that in cases where a derivative contract is restructured, the mark-to-market value of the contract on the date of restructuring should be cash settled. In this context, RBI has clarified that cash settlement of only the change in mark-to-market value of the restructured derivative contract is required.

It may, however, be ensured that the restructuring of the derivative contract is carried out at prevalent market rates and not on the basis of off-market rates.

Review of prudential norms: Risk weights for exposures to corporates, AFCs and NBFC-IFCs

At present, unrated exposures to corporates, AFCs and NBFC-infrastructure finance company (NBFC-IFCs) attract a risk weight of 100%. On a review, it has now been decided to make the following modifications to the risk weights applicable to unrated exposures:

- With effect from 30 June 2017, all unrated claims on corporates, AFCs and NBFC-IFCs having aggregate exposure from a banking system of more than 200 crore INR will attract a risk weight of 150%.
- However, claims on corporates, AFCs and NBFC-IFCs having aggregate exposure from a banking system of more than 100 crore INR, which were rated earlier and subsequently have become unrated, will attract a risk weight of 150% with immediate effect.

Master Directions on Frauds – Classification and Reporting by commercial banks and select financial institutions (FIs)

RBI has issued Master Directions on Frauds – Classification and Reporting by commercial banks and select FIs. The provisions of these directions will apply to scheduled commercial banks (excluding RRBs) and select FIs operating in India. These directions are issued with a view to providing a framework to banks, enabling them to detect and report frauds early and taking timely consequent actions like reporting to investigative agencies so that fraudsters are brought to book early, examining staff accountability and do effective fraud risk management. These directions also aim to enable faster dissemination of information by RBI to banks on the details of frauds, unscrupulous borrowers and related parties based on banks' reporting so that necessary safeguards/preventive measures by way of appropriate procedures and internal checks may be introduced and caution exercised while banks deal with such parties by banks.

ICAI

ICAI issues revised Guidance Note on Reports or Certificates for Special Purposes

The Auditing and Assurance Standards Board of ICAI has issued a Guidance Note on Reports or Certificates for Special Purposes (Revised 2016). This Guidance Note supersedes the Guidance Note on Audit Reports and Certificates for Special Purposes, issued by ICAI in 1984.

Amendment to AS 2, 4, 6, 10, 13, 14, 21 and 29 issued by ICAI, pursuant to issuance of amendments to accounting standards by MCA

The Council of ICAI noted that MCA has notified Companies (Accounting Standards) Amendment Rules, 2016. With a view to harmonising the accounting standards issued by ICAI for non-corporate entities and the amendments to the accounting standards notified by the central government, the council decided that the amendments notified by the central government, after appropriate changes, will also be incorporated in the accounting standards issued by ICAI. In view of the above, the following changes have been made in the accounting standards issued by ICAI:

- AS 6 - Depreciation Accounting stands withdrawn.

The following accounting standards are amended:

- AS 2 - Valuation of Inventories.
- AS 4 - Contingencies and Events Occurring after the Balance Sheet Date.
- AS 10 - PP&E.
- AS 13 - Accounting for Investments.
- AS 14 - Accounting for Amalgamations.
- AS 21 - Consolidated Financial Statements.
- AS 29 - Provisions, Contingent Liabilities and Contingent Assets.

These amendments will come into effect in respect of accounting periods commencing on or after 1 April 2017.

Withdrawal of the Application Guide on the Provisions of Schedule II to the Companies Act, 2013

The Application Guide on the Provisions of Schedule II to the Companies Act, 2013, is no longer effective and stands withdrawn from the date the Guidance Note on Accounting for Depreciation in Companies in the context of Schedule II to the Companies Act, 2013, became applicable, i.e. for accounting periods beginning on or after 1 April 2016.

Guidance note on audit of consolidated financial statements

ICAI has issued a revised guidance note on the audit of consolidated financial statements. This guidance supersedes the earlier guidance note on the subject matter issued in 2003. The revised guidance note has been issued considering the significant developments in corporate law and accounting standards.

Clarification on the difference in requirements relating to auditor's rotation under SQC 1 vis-à-vis Companies Act, 2013

The Council of ICAI considered the issue regarding the difference in requirements relating to auditor's rotation under the SQC 1, 'Quality Control for Firms that Perform Audits and Reviews of Historical Financial Information, and Other Assurance and Related Services Engagements' issued by ICAI vis-à-vis the Companies Act, 2013. At the meeting, the Council noted the following points:

a. In case of audits of listed entities, paragraph 27 of SQC 1 requires rotation of engagement partner after a predefined period, normally not more than seven years.

b. Since SQC 1 is applicable from 1 April 2009, the provisions regarding the rotation of engagement partner will be due from 1 April 2016 during the transition phase.

c. Since the Companies Act, 2013, is applicable from 1 April 2014 and the existing companies have been given a relaxation of 3 years to comply with requirement of auditor's rotation, the provisions regarding auditor's rotation would be due from 1 April 2017 during the transition phase. Hence, there is a difference of 1 year in the requirement of auditor's rotation between SQC 1 vis-à-vis the Companies Act, 2013, during the transition phase of implementation of the Companies Act, 2013.

On consideration of the matter, the council decided to issue a clarification on the issue and provide relaxation in the requirement of rotation of engagement partner given in paragraph 27 of SQC 1 for the transition phase (i.e., one time only for FY 2016–17).

Exposure draft of Guidance Note on Reports in Company Prospectuses

The Auditing and Assurance Standards Board of ICAI has issued an exposure draft of the proposed Guidance Note on Reports in Company Prospectuses. The proposed guidance note, once issued, will be applicable for providing guidance to issuers in relation to the preparation of financial information to be included in the prospectus in case of an IPO and to auditors in relation to reporting requirements that are required in such a scenario. This proposed guidance note will also be applicable to other type of filings for the issue of securities, such as letter of offer (in case of right issue) and placement document (QIBs), to the extent relevant. The exposure draft was open for comments till 10 October 2016.

Background Material on Model GST Law

ICAI has issued Background Material on Model GST Law. The material contains a section-wise analysis of provisions of the Model GST Law along with relevant illustrations to explain the law.

IRDAI

IRDAI (Investment) Regulation, 2016, and master circular thereon

The IRDAI issued IRDAI (Investment) Regulation, 2016, on 1 August 2016. As the regulations mandate that certain systems and process be put in place, IRDAI (Investment) Regulations, 2016 (Regulations), will be effective from 31 March 2017. Thus, insurers will report compliance to the Regulations in the regulatory periodical submissions from quarter ended 31 March 2017. IRDAI has issued a master circular to make necessary amendments to the circulars and guidelines issued earlier, which will serve as a one stand point reference. IRDAI has directed insurers to place the Regulations, Investment - Master Circular on IRDAI (Investment) Regulations, 2016, before their board in their next meeting and appraise their Board of the changes that have been made in the investment regulations.

Guidance Note on Preparation of Investment Returns

To bring consistency in the data filed through electronic submission, IRDAI issued a 'Guidance Note on Preparation of Investment Returns'.

CBDT

Report regarding framework for computation of book profit for the purposes of levy of MAT under section 115JB of the Income-tax Act, 1961, for Ind AS compliant companies in the year of adoption and thereafter

A committee constituted to suggest the framework for the computation of book profit for the purposes of levy of MAT under section 115JB of the Income-tax Act, 1961, for Ind AS compliant companies in the year of adoption and thereafter had submitted its report dated 18 March 2016 regarding the said framework. The report of the committee was placed in the public domain for comments from the general public and stakeholders which were subsequently forwarded to the committee for examination.

After evaluating the recommendations/suggestions received from stakeholders, the committee submitted its second report dated 23 July 2016. The report discussed the following topics:

a. Fixed assets: Adjustments to retained earnings.
b. Leases: Straight-lining of lease rentals.
c. Investments: Fair value adjustments through profit and loss account.
d. Other adjustments to book profits as per para 10(III) of the report dated 18 March 2016.

The report was placed on the website of the Income Tax Department for public comments.

Revised ICDS

CBDT, through its notification dated 29 September 2016, notified revised ICDS and repealed its earlier notification dated 31 March 2015. The revised ICDS shall apply to all assessees (other than an individual or a Hindu undivided family which is not required to get its accounts of the previous year audited in accordance with the provisions of section 44AB of the Income-tax Act, 1961) following the mercantile system of accounting for the purposes of computation of income chargeable to income tax under the head 'Profits and gains of business or profession' or 'Income from other sources'. The notification shall apply to AY 2017–2018 and subsequent AYs.

There are no amendments to three ICDSs related to accounting policies, government grants and provisions, contingent liabilities, and contingent assets. All other ICDSs have been amended.

Further, CBDT, through its notification, has also amended the tax audit report Form No. 3CD by inserting a new sub-clause in the form to provide details of the adjustments with respect to ICDS and disclosures as per ICDS.

IFRS: IASB

IASB issues amendments to IFRS 4, 'Insurance contracts' regarding the implementation of IFRS 9, 'Financial instruments'

On 12 September 2016, IASB published an amendment to IFRS 4, 'Insurance contracts'. This addresses the concerns of insurance companies about the different effective dates of IFRS 9, 'Financial instruments', and the forthcoming new insurance contracts standard. The amendment to IFRS 4 provides two different solutions for insurance companies: a temporary exemption from IFRS 9 for entities that meet specific requirements (applied at the reporting entity level); and the 'overlay approach'. Both approaches are optional. IFRS 4 (including the amendments that have now been issued) will be superseded by the forthcoming new insurance contracts standard. Accordingly, both the temporary exemption and the overlay approach are expected to cease to be applicable when the new insurance standard becomes effective.

The amended standard will give:

- all companies that issue insurance contracts the option to recognise in OCI, rather than profit or loss, the volatility that could arise when IFRS 9 is applied before the new insurance contracts standard is issued; and
- companies whose activities are predominantly connected with insurance an optional temporary exemption from applying IFRS 9 until 2021. The entities that defer the application of IFRS 9 will continue to apply the existing financial instruments standard—IAS 39.

US GAAP: FASB

Income tax disclosure framework

On 26 July 2016, FASB issued a proposed ASU, Disclosure Framework - Changes to the Disclosure Requirements for Income Taxes, which would add new and modify existing tax disclosures—calling for more disaggregation in some cases.

Although many of the proposed disclosures codify existing SEC requirements, certain of the new disclosures would require companies to disclose information that was not previously publicly available. Compiling the necessary information, particularly for multinational corporations, may be challenging as it would require significant effort.

New cash flow guidance

On 26 August 2016, FASB issued ASU 2016-15, Statement of Cash Flows (Topic 230), a consensus of FASB's Emerging Issues Task Force. The new guidance is intended to reduce diversity in practice in how certain transactions are classified in the statement of cash flows. ASU addressed how the following cash transactions are presented:

1. debt prepayment or debt extinguishment costs;
2. settlement of zero-coupon debt instruments;
3. contingent consideration payments made after a business combination;
4. proceeds from the settlement of insurance claims;
5. proceeds from the settlement of corporate-owned life insurance policies, including bank-owned life insurance policies;
6. distributions received from equity method investments; and
7. beneficial interests in securitisation transactions.

It also addresses how to present cash flows with aspects of multiple classifications. The standard is effective for financial statements issued for fiscal years beginning after 15 December 2017 and interim periods within those fiscal years. Early adoption is permitted, provided that all of the amendments are adopted in the same period.

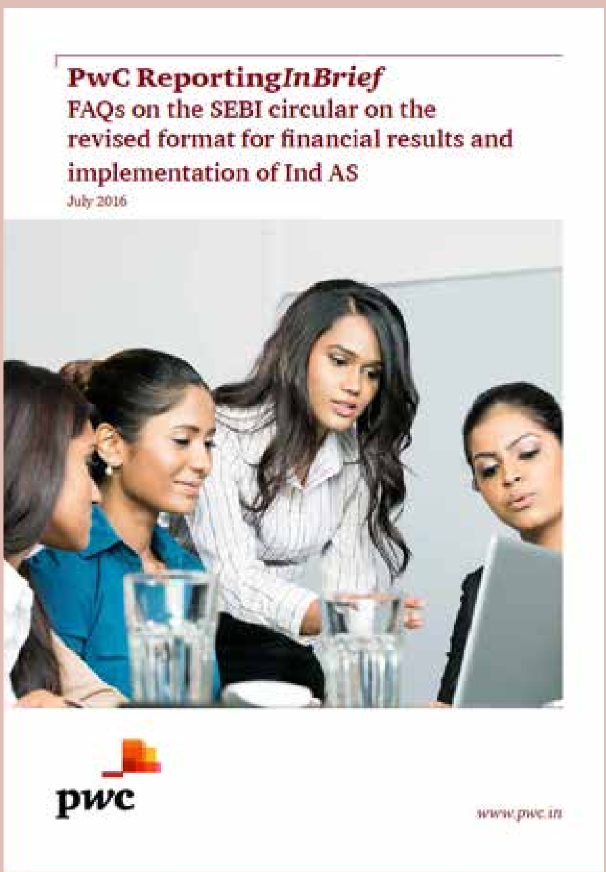
FASB proposes changes to the hedge accounting model

On 8 September 2016, FASB issued a proposed ASU to ASC 815 (Derivatives and Hedging). The proposed guidance will impact the hedge accounting guidance for both financial and nonfinancial hedging relationships. The goals are to improve the alignment between hedge accounting and a reporting entity's risk management objectives and to simplify hedge accounting for preparers. The proposed guidance, if finalised, will significantly change what qualifies for hedge accounting, how it is documented, how hedge effectiveness is assessed and hedge ineffectiveness is measured, and how the hedging results are presented and disclosed in the financial statements.

Abbreviations

AFC	Asset finance companies
AGM	Annual general meeting
AIFI	All India Term Lending and Refinancing Institutions
AS	Accounting Standard
ASU	Accounting Standard Update
ASB	Accounting Standard Board
AY	Assessment year
CBDT	Central Board of Direct Taxes
CGU	Cash-generating unit
FASB	Financial Accounting Standards Board
GAAP	Generally Accepted Accounting Principles
GN	Guidance Note
IASB	International Accounting Standards Board
ICAI	Institute of Chartered Accountants of India
IFCFR	Internal financial control over financial reporting
IFRS	International Financial Reporting Standards
Ind AS	Indian Accounting Standards
IRDA	Insurance Regulatory and Development Authority
ITFG	Ind AS Transition Facilitation Group
LLP	Limited liability partnership
MAT	Minimum alternate tax
MCA	Ministry of Corporate Affairs
NBFC	Non-banking financial company
OCI	Other comprehensive income
QIB	Qualified institutional buyer
PP&E	Property, plant and equipment
RBI	Reserve Bank of India
SA	Standards on Auditing
SC/RC	Securitisation companies/ reconstruction companies
SEBI	Securities Exchange Board of India
SPV	Special purpose vehicle
SQC	Standard on quality control
US GAAP	US Generally Accepted Accounting Principles
VAT	Value-added tax

Publications
Previous publications

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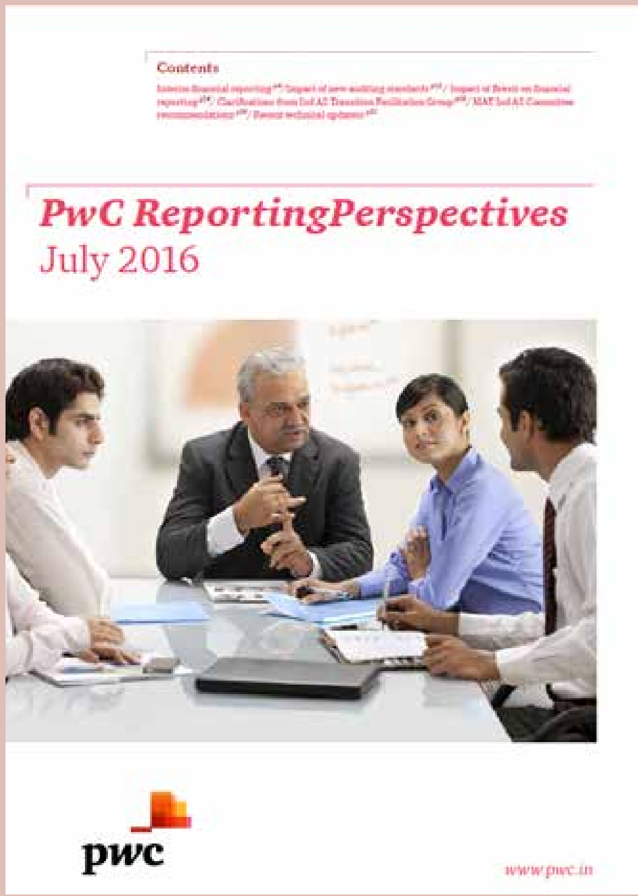
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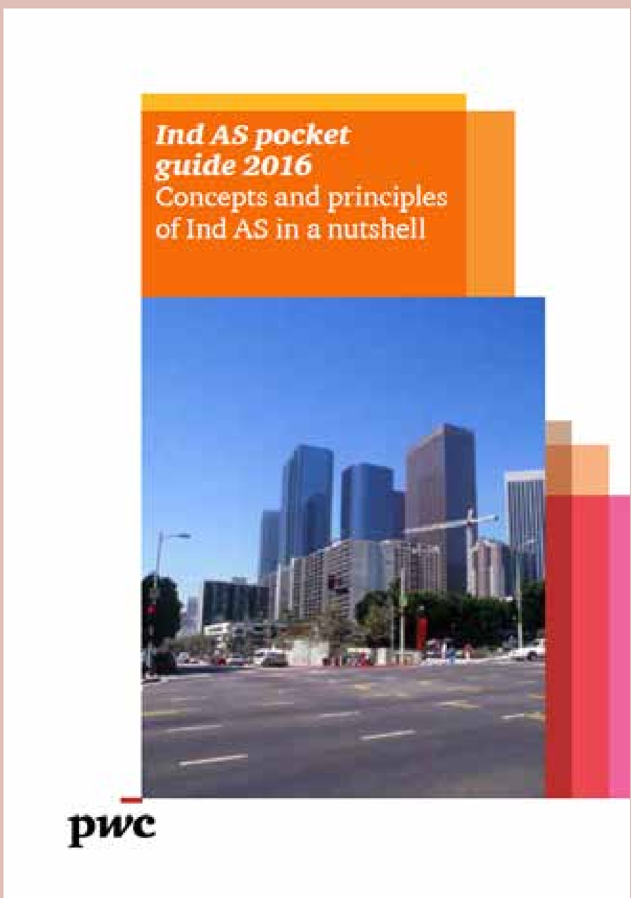
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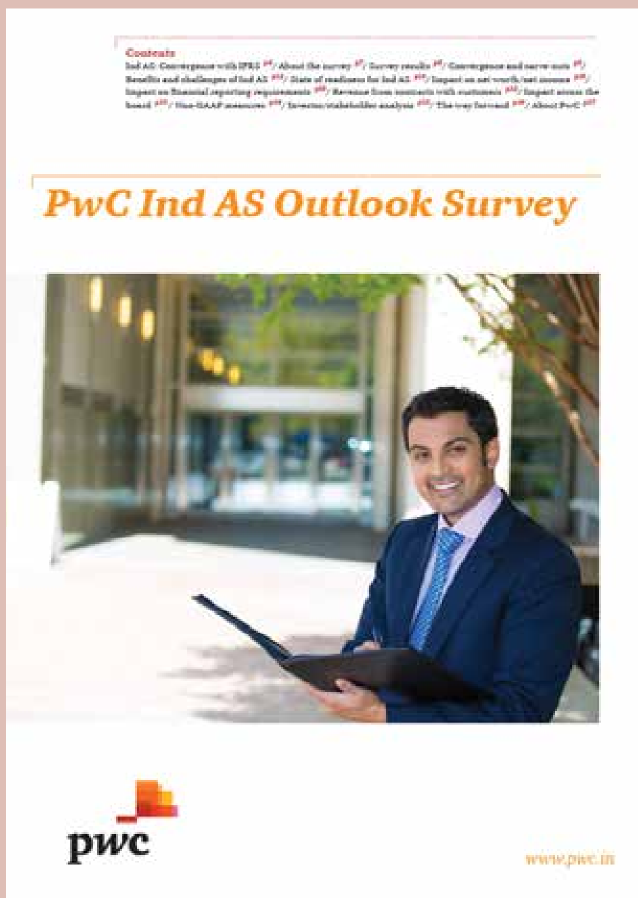
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