Indian Accounting Standards (Ind AS)

Overview

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- Ind AS - conceptual changes
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Background and Roadmap for implementing Ind AS
Background

- Ind AS was introduced with a view to enhance acceptability and transparency of the financial information communicated by the Indian corporates through their financial statements throughout the globe.

- This move towards IFRS was subsequently accepted by the Government of India and was announced by the Hon’ble Finance Minister of India, Arun Jaitley, in his Budget Speech in July 2014.

“There is an urgent need to converge the current Indian accounting standards with the International Financial Reporting Standards (IFRS). I propose for adoption of the new Indian Accounting Standards (Ind AS) by the Indian companies from the financial year 2015-16 voluntarily and from the financial year 2016-17 on a mandatory basis. Based on the international consensus, the regulators will separately notify the date of implementation of Ind AS for the Banks, Insurance companies etc. Standards for the computation of tax would be notified separately“.
Roadmap for implementing Ind AS

**Phase I**
- Companies whose equity or debt securities are listed or are in the process of listing on any stock exchange in India or outside India (listed companies) and having net worth of Rs.500 crores or more
- Unlisted companies having a net worth of Rs.500 crores or more
- Holding, subsidiary, joint venture or associate companies of the listed and unlisted companies covered above

**Phase I - NBFC**
- All Scheduled commercial banks (other than UCBs & RRBs)
- All India Term-lending Refinancing Institutions
- NBFCs with net worth of Rs. 500 crores or more

**Phase II**
- Listed companies having net worth of less than Rs.500 crore
- Unlisted companies having net worth of Rs.250 crore or more but less than Rs.500 crore
- Holding, subsidiary, joint venture or associate companies of the listed and unlisted companies covered above

**Phase II - NBFC**
- All listed NBFCs (or in the process of listing) & not covered in Phase I above
- All unlisted NBFCs with net worth of Rs.250 crores or more but less than Rs. 500 crores
Roadmap for implementing Ind AS contd..

Insurance companies:

IRDAI vide press release dated June 28, 2017 has deferred the implementation of Ind AS for the Insurance Sector in India for a period of two years and the same shall now be implemented effective from 2020-21.

Scheduled Commercial Banks (excluding Regional Rural Banks):

RBI vide press release dated April 05, 2018 has deferred the implementation of Ind AS for the Scheduled Commercial Banks (excluding Regional Rural Banks) for a period of one year and the same shall now be implemented effective from 1st April 2019.

Further, RBI vide notification dated March 22, 2019 has again deferred the implementation of Ind AS for the Scheduled Commercial Banks (excluding Regional Rural Banks) till further notice.
Ind AS – conceptual changes
Major Concepts in Ind AS

Fair Value Measurement (Ind AS 113)

1. Determine whether item is in scope of Ind AS 113
2. Establish parameters
   - Identify the item being measured
   - Identify unit of account & unit of valuation
   - Identify the market parameters and identify the market
3. Select appropriate valuation approaches and techniques
   - Market approach
   - Income approach
   - Cost approach
4. Measure Fair value
   - FV at initial recognition
   - Highest and Best use
   - Liabilities and own Equipment
   - Portfolio measurement exceptions
   - Inactive markets
5. Determine inputs to value fair value
   - Level 1
   - Level 2
   - Level 3
6. Disclose information about FVM
Major Concepts in Ind AS contd..

Expected Credit loss method

• “Expected credit loss” is a credit loss impairment model which focuses on recognizing the provisions based on expected losses (or credit losses) and not on incurred losses.

• The credit loss is discounted at effective interest rate or any other appropriate adjusted discount rate. The weighted average of the cash flows the entity expects to realize is then assessed to reach on the expected credit loss.

\[
\text{Cash flow the entity expects to receive} - \text{Cash flow due to the entity} = \text{Credit Loss}
\]

Effective Interest Rate (Ind AS 109)

• Time value of money – INR 100 received next year is less in value compared to INR 100 received today!
Major Concepts in Ind AS contd..

**Other Comprehensive Income**

- Ind AS requires the statement of profit and loss to be presented in two parts:
  - Comprehensive income part (CI)
  - other comprehensive income part (OCI).

- It contains income and expense (including reclassification adjustments) that are not recognized in profit and loss as required or permitted by other Ind AS.

- The reason for presentation of other comprehensive income is that there are wide range of activities which are incidental to the operations of an organization in due course of its business which lead to non-cash income or losses.

- OCI consist of following items:

<table>
<thead>
<tr>
<th><strong>Items that can be recycled</strong></th>
<th><strong>Items that cannot be recycled</strong></th>
</tr>
</thead>
<tbody>
<tr>
<td>Gain or loss on change in Fair value of investment in Debt instrument</td>
<td>Gain or loss on change in Fair value of Equity instrument</td>
</tr>
<tr>
<td>Change in FV of cash flow hedge reserve</td>
<td>Actuary gain or loss</td>
</tr>
<tr>
<td>Exchange on foreign operations</td>
<td>Revaluation reserve</td>
</tr>
</tbody>
</table>
Major Concepts in Ind AS contd.

Compound Financial Instrument (Ind AS 9 and Ind AS 32)

• Compound Financial Instrument is an instrument which contains whose terms may be structured in a way that it contains both equity and liability components.

• Both the Liability and Equity component of a CFI is required to be separately accounted for which is the best example of following the principles of “substance over form”.

• Example : A convertible bond, either mandatorily or at the option of the holder, into fixed number of equity shares of the issuer

• At initial recognition, the instrument is recognized as follows:
  ✓ FV of the liability component is calculated, and is considered as the initial carrying amount of the liability component.
  ✓ FV of the liability component calculated above is deducted from FV of the instrument as a whole, with the resulting residual amount being recognized as equity component.
Hedge Accounting

- Hedge accounting is applied by identification of hedged item (exposed to one or more risks) then identifying the hedging instrument (i.e., a derivative or non-derivative to offset risk in cash flow/fair value of hedged item) and if the hedging relationship is effective and it meets the requisite criteria for hedge accounting i.e. establishing type of hedge:
  - Fair value hedge
  - Cash flow hedge
  - Hedge of net investment in foreign operations
Key Takeaways of Ind AS
Key takeaways of Ind AS

Ind AS 1 Presentation of Financial Statement:

- Components of financial statements
- True and fair presentation and compliance with Ind AS
- Statement of profit and loss having two parts viz. profit or loss and other comprehensive income
- Expense recognition on the basis of nature, not function.

Ind AS 2 Inventories:

- Inventory for service provider to be included in the scope for example: cost of personnel, wages and other attributable overheads.
- Deferred credit purchase i.e. bifurcation of finance cost from the part of inventory in case when credit period allowed is more than normal credit period
- Treatment of Machinery spares provided
- Standard cost method and retail method for measurement of inventories
Key takeaways of Ind AS contd..

Ind AS 7 Statement of Cash Flow:
- Inclusion of Bank overdraft repayable on demand as part of Cash and cash equivalent
- Use of direct method
- No requirement for a cash flow relating to extraordinary items separately
- Disposal of stake in subsidiary not resulting in loss of control to be covered in financial activities

Ind AS 8 Accounting Policies, Changes in Accounting Estimates and Errors:
- Change in Accounting policy is allowed for better presentation or if change is to implement an Ind AS requirement (earlier change was only brought as per requirement of statutory compliance)
- Change in accounting policy to be retrospectively accounted for unless impracticable. Cumulative profit/loss to be adjusted with retained earnings by corresponding change in value of asset/liability and the effect to be provided in the statement of changes in equity and not profit and loss
- Prior period items to be rectified retrospectively and effect of such change on asset and liability to be adjusted in retained earnings and not profit or loss account.
- Consistency in applying selected accounting policy
Key takeaways of Ind AS contd..

Ind AS 16 Property, Plant and Equipment:

- PPE to be recognized in books if:
  - Probability of future economic benefit to flow to the enterprise; and
  - Respective cost can be measured reliably.

- Initial expenditure and subsequent expenditure to be treated in same manner.

- Component approach to be applied in recognition of PPE

- Asset retirement obligation to be considered at the beginning and as per present value technique, the corresponding liability amount to be increased every year using effective interest rate (EIR) and accordingly settlement to be made at the time of retirement

- Capitalization of Inspection Cost (also decapitalization of existing amount of earlier inspection cost)

- After initial recognition of a PPE, Ind AS 16 requires subsequent measurement at:
  - **The Cost Model**: Asset carried at cost less accumulated depreciation and impairment losses
  - **The Revaluation Model**: The asset is carried at a revalued amount, being its fair value at the date of the revaluation, less subsequent depreciation, provided that fair value can be measured reliably

- Useful life, residual value and method of depreciation to be reviewed each year and the effect should be prospective and treated as change in accounting estimate
Key takeaways of Ind AS contd..

Ind AS 19 Employee Benefits:

- Actuarial gains and losses to be accounted for in OCI

- Discount rate to be used for foreign subsidiary, associates, Joint Venture to be high quality corporate bond rate if available, or else government bond rate to be used

- Presentation of three components of “defined benefit cost”:
  - Service cost (current, past, curtailment loss / (gain), and settlement loss / (gain) in profit or loss
  - Net Interest in profit or loss
  - Re-measurements (actuarial gains, the return on plan assets (excl. net interest), change in the effect of the asset ceiling) in other comprehensive income (OCI).
Key takeaways of Ind AS contd..

Ind AS 21 The Effects of Changes in Foreign Exchange Rates:

• Exclusion of Financial instruments such as forward contract from its purview and provided in Ind AS 9 Financial Instruments
• No distinction between integral and non-integral foreign operations
• Concept of functional currency and presentation currency introduced
• Translation difference to be recorded and disclosed in OCI
Key takeaways of Ind AS contd..

Ind AS 23 Borrowing Cost:

- Considering substantial period of time left at the discretion of the management
- No mention of amortization of other ancillary cost, discounts and premium related to borrowing since Ind AS uses Effective Interest Rate (EIR) Method and considers the loan to be a Held to maturity (HTM) Liability
- Capitalization rate of the borrowing to be disclosed in the notes to accounts
Key takeaways of Ind AS contd..

Ind AS 24 Related Party Disclosures:

- Alteration in the definition of close members
- KMP of the parent to be included in Related party relationship
- Two Joint Ventures (JV) of the same co-venture are related parties to each other
- Associate and JV of the same party are related
- Defined benefit Plans (enterprises managing retirement benefit plans of the employees) of an entity to be included in the list of related parties.
- Remuneration to Key Management Personnel to be disclosed section wise
- Meaning of Control, significant Influence, joint control derived from Ind AS 110, Ind AS 28 and Ind AS 111 respectively
Key takeaways of Ind AS contd..

**Ind AS 33 Earnings per Share:**

- No requirement of reporting EPS including extraordinary items and EPS excluding extraordinary items separately.
- Presentation of separate EPS for continuing operations and discontinuing operations

**Ind AS 34 Interim Financial Reporting:**

- Prescribed the minimum content of an interim financial report and to prescribe the principles for recognition and measurement in complete or condensed financial statements for an interim period
- Interim period – financial period shorter than full year
- Interim financial report – either a complete (as described in IND AS 1) or condensed set of financial statements
Key takeaways of Ind AS contd..

Ind AS 36 Impairment of Assets:

- Ind AS 36 also to apply to impairment of Investment in associates subsidiaries and J.V.
- Goodwill to be put to test of impairment every year, not amortized. Prohibition on reversal of impairment of Goodwill
- Goodwill to be allocated with particular Cash Generating Unit (CGU)
Key takeaways of Ind AS contd..

Ind AS 40 Investment Property:

- Provides detailed guidelines on the accounting of Investment Property.
- Initially to be valued at cost, subsequently to be valued using cost model.
- Revaluation model is not allowed however, entity is required to estimate the fair value of the asset for disclosure purposes.
Key takeaways of Ind AS contd..

Ind AS 38 Intangible Assets:

• An intangible asset with infinite life must be put to test of impairment every year
• If the Legal life is longer than useful life, still useful life to be used for purpose of amortization
• Intangibles to be subsequently measured at either:
  ✓ Cost Model
  ✓ Revaluation Model
Key takeaways of Ind AS contd..

**Ind AS 41 Agriculture:**

- Ind AS 41 covers:
  - Biological assets
  - Agricultural produce
  - Government grants

- No depreciation accounting required since the assets are already measured at fair value.
Key takeaways of Ind AS contd.

**Ind AS 101 First-time Adoption of Indian Accounting Standards:**

- Ind AS 101 applies to the first set of financial statements that contain an explicit and unreserved statement of compliance with Ind AS.
- Ind AS 101 applies to any interim financial statements for a period covered by those first financial statements that are prepared under Ind AS.
- Previous GAAP is defined as the basis of accounting that a first-time adopter used for its reporting requirements in India immediately before adopting IND AS.
- Recognize all assets and liabilities whose recognition is required by Ind AS.
- Derecognize assets and liabilities if Ind AS do not permit such recognition.
Key takeaways of Ind AS contd..

**Ind AS 102 Share-based Payment:**

- Detailed guidance available for accounting and disclosures of equity-settled and cash-settled transactions
- Ind AS 102 also covers share based payment transactions with non-employees as well

![Diagram showing the flow of goods/services and share-based payment to and from entity and supplier.](Diagram Image)
Key takeaways of Ind AS contd..

**Ind AS 103 Business Combination:**

- Only one method of amalgamation i.e., acquisition method (similar to purchase method)
- Contingent considerations to be considered in case of amalgamation
- Assets acquired in case of a Business combination to be recorded at fair value only
- Concept of legal acquirer and accounting acquirer introduced in cases of reverse merger
- Consideration of non-controlling interest in a business combination
Key takeaways of Ind AS contd..

**Ind AS 105 Non-current Assets Held for Sale and Discontinued Operations:**

- **Discontinued operation** – A component of an entity that either has been disposed off or is classified as held for sale and either:
  - ✓ Represents a separate major line of business or geographical areas part of a single coordinated plan to dispose of a separate major line of business or geographical area of operations
  - ✓ Is a subsidiary acquired exclusively with a view to resale
- **Applies to all recognized non-current assets and disposal groups of an entity that are:** held for sale; or Held for distribution to owners
Key takeaways of Ind AS contd..

**Ind AS 109 Financial Instruments :**

- Ind AS 109 introduces a single classification and measurement model for financial assets, dependent on both:
  - The entity's business model objective for managing financial assets
  - The contractual cash flow characteristics of financial assets

- Ind AS 109 removes the requirement to separate embedded derivatives from financial asset host contracts (it instead requires a hybrid contract to be classified in its entirety at either amortized cost or fair value) Separation of embedded derivatives has been retained for financial liabilities (subject to criteria being met).

- Financial Assets are classified as either:
  - Amortized cost
  - Fair value through profit or loss
  - Fair Value through other comprehensive income
## Major impact of Ind AS on listed companies

<table>
<thead>
<tr>
<th>Under existing standards (IGAAP)</th>
<th>New accounting (Ind AS)</th>
<th>Impact</th>
</tr>
</thead>
<tbody>
<tr>
<td>Most companies having employee stock option based on intrinsic value</td>
<td>Mandates ESOP cost booked under fair value accounting</td>
<td>Likely to increase employee cost</td>
</tr>
<tr>
<td>Proposed dividend is recognized in the same year</td>
<td>Proposed dividend in a year when approved by shareholders</td>
<td>Likely to increase the year end book value of the company. This may lower return on equity (ROE) of high-dividend paying companies.</td>
</tr>
<tr>
<td>Business combination – option to recognize assets at book value</td>
<td>Asset and liability to be recognized at fair value and continent liabilities to be accounted at fair value. Goodwill value to be tested annually.</td>
<td>Companies having high goodwill in balance sheet will see volatilities in their earnings</td>
</tr>
<tr>
<td>Current investment valued at cost or market value</td>
<td>Need to be valued at fair value</td>
<td>Greater volatility in other income</td>
</tr>
<tr>
<td>Redeemable preference share treated as part of equity</td>
<td>Redeemable Preference share will be treated as liability, preference dividend will be treated as interest cost</td>
<td>Higher debt to equity and lower EPS</td>
</tr>
<tr>
<td>Major repair charged as expenses</td>
<td>Allowed to capitalized</td>
<td>Could lead to lower EPS</td>
</tr>
<tr>
<td>Revenues calculated net of excise duty (not applicable presently)</td>
<td>Revenues will be calculated by adding excise duty (not applicable presently)</td>
<td>Higher revenue, lower margin and EPS neutral.</td>
</tr>
</tbody>
</table>
Ind AS 115 – Revenue Recognition
A contract is an agreement between two or more parties that creates enforceable rights and obligations. A contract can be written, oral, or implied by an entity’s customary business practices. For a contract to exist the following five criteria must be met:

- The parties to the contract have approved the contract
- The entity can identify each party’s rights
- The entity can identify the payment terms
- The contract has commercial substance
- It is probable the entity will collect the amount to which it expects to be entitled.

New revenue recognition requirements

Five-step model for recognizing revenue

1. Identify the contract with the customer
2. Identify the performance obligations
3. Determine the transaction price
4. Allocate the transaction price
5. Recognize revenue when (or as) performance obligations are satisfied
**New revenue recognition requirements**

**Five-step model for recognizing revenue**

1. Identify the contract with the customer
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3. Determine the transaction price
4. Allocate the transaction price
5. Recognize revenue when (or as) performance obligations are satisfied

- A performance obligation is the promise to transfer to the customer a good or service (or bundle of goods or services) that is distinct.
- Distinct goods and services should be accounted for as separate units of account.
- Entities need to determine if a good or service (or bundle of goods or services) is “capable of being distinct” and “distinct in the context of the contract.”
- A series of substantially the same goods or services for which control transfers over time and that have the same pattern of transfer is accounted for as a single performance obligation.
Transaction price is the amount the entity expects to be entitled to in exchange for transferring promised goods or services to the customer.

The transaction price may include fixed amounts, variable amounts, or both.

To determine the transaction price, entities shall consider the effects of the following:

- Variable consideration
- The constraint on estimates of variable consideration
- Significant financing components
- Noncash consideration
- Consideration payable to the customer.
New revenue recognition requirements

Five-step model for recognizing revenue

1. Identify the contract with the customer
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3. Determine the transaction price
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5. Recognize revenue when (or as) performance obligations are satisfied

• The transaction price (from step 3) is allocated to each performance obligation identified (from step 2).
• Depending on the specific circumstances, one of the following approaches would be used to allocate the transaction price to the performance obligations:
  ✓ On the basis of each performance obligation’s stand-alone selling price
  ✓ Allocation of a discount or variability to a specific performance obligation (or a bundle of specific performance obligations) if certain criteria are met.
New revenue recognition requirements

Five-step model for recognizing revenue

1. Identify the contract with the customer
2. Identify the performance obligations
3. Determine the transaction price
4. Allocate the transaction price
5. Recognize revenue when (or as) performance obligations are satisfied

• Requires consideration of the following:
  ✓ Recognition of revenue when (or as) control of the good or service is passed to the customer (at a point in time or over time)
  ✓ Over time: Specific criteria needed to be met for satisfying performance obligations and recognizing revenue over time
    o If recognizing revenue over time, a measure of progress should be used to determine the pattern of when to recognize revenue
  ✓ Point in time: If revenue is not recognized over time, it is recognized at a point in time. There are indicators of when performance obligations are satisfied and revenue recognized for performance obligations satisfied at a point in time.
Ind AS 116 – Leases
Overview

Effective date: 1 January 2019

Limited changes to scope of IAS 17
Enhanced guidance on identifying a lease

Lessee accounting

- Operating lease vs Finance lease
- Right-of-use (ROU) asset and Lease liability

Lessor accounting

- Operating lease vs Finance lease

IAS 17 vs IFRS 16
## Financial Statement Impact

### Old standard

<table>
<thead>
<tr>
<th>Income statement</th>
<th>FY 20xx $</th>
</tr>
</thead>
<tbody>
<tr>
<td>Lease payments</td>
<td>xxx</td>
</tr>
<tr>
<td>EBITDA</td>
<td>xxx</td>
</tr>
<tr>
<td>Profit before tax</td>
<td>xxx</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Balance Sheet</th>
<th>FY 20xx $</th>
</tr>
</thead>
</table>

### New standard

<table>
<thead>
<tr>
<th>Income statement</th>
<th>FY 20xx $</th>
</tr>
</thead>
<tbody>
<tr>
<td>Low-value/short-term leases</td>
<td>xxx</td>
</tr>
<tr>
<td>EBITDA</td>
<td>xxx</td>
</tr>
<tr>
<td>Depreciation and amortisation</td>
<td>xxx</td>
</tr>
<tr>
<td>Finance cost</td>
<td>xxx</td>
</tr>
<tr>
<td>Profit before tax</td>
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<th>Balance Sheet</th>
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<tr>
<td>Lease assets</td>
<td>xxx</td>
</tr>
<tr>
<td>Lease liabilities</td>
<td>xxx</td>
</tr>
</tbody>
</table>
Definition of a Lease

Is there an identified asset?
- Yes
- No

Does the customer have the right to obtain substantially all of the economic benefits of the asset throughout the period of use?
- Yes
- No

Does the customer, the supplier, or neither party have the right to direct how and for what purpose the asset is used throughout the period of use?
- Yes
- Supplier
- Neither

Does the customer have the right to operate the asset throughout the period of use, without the supplier having the right to change those operating instructions?
- No

Did the customer design the asset in a way that predetermines how and for what purpose the asset will be used throughout the period of use?
- Yes
- No

Contract contains a lease
- Yes

Contract does not contain a lease
- No
Exemptions

Accounting policy choice:
Apply Ind AS 116 or straight-line the expense

- Short-term leases (12 months or less)
- A lease that contains a purchase option is not a short-term lease
- Election by class of underlying asset

- Low-value leases
- Assessment on an absolute basis
- Election on a lease-by-lease basis
Determination of ROU Asset

NPV = Lease Liability

- Fixed payments less incentives
- Expected residual value guarantee
- Penalty for terminating (if reasonably certain)
- Variable payments (e.g., CPI/rate)
- Exercise price of purchase option (reasonably certain)
- Estimated cost for dismantling restoring asset
- Payments less incentives before commencement date
- Lease Liability
- Initial direct costs

ROU Asset
Questions
"Drat. My talk about obsolete accounting standards must have been too exciting for them."

Thank You