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Voices on Reporting

22 July 2015

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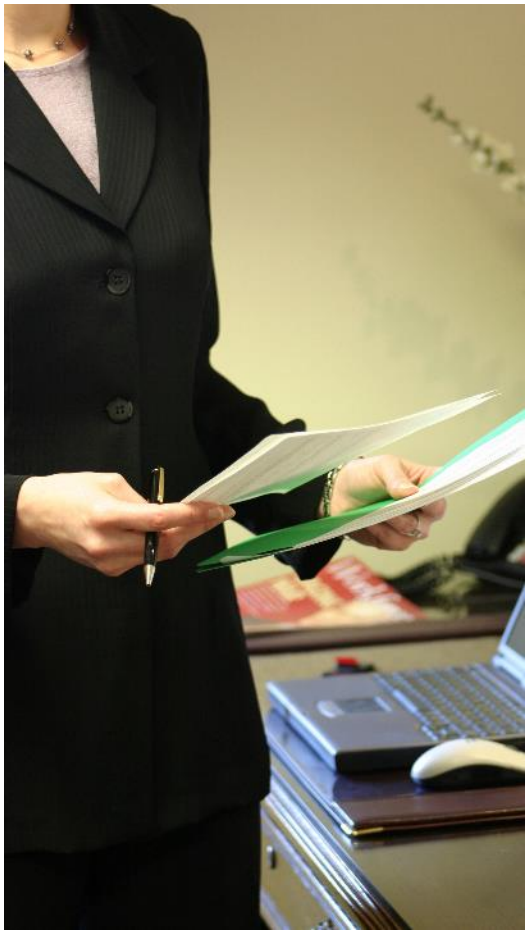
Welcome



- Series of knowledge sharing calls
- Covering current and emerging reporting issues
- Scheduled towards the end of each month
- Look out for our Accounting and Auditing Update, IFRS Notes and First Notes publications

Your speaker

Nirav Patel
Director
Accounting Advisory Services
KPMG in India

Agenda

1. **Overview of Ind AS 110, *Consolidated Financial Statements* and Ind AS 27, *Separate Financial Statements***
2. Key differences between AS 21, *Consolidated Financial Statements* and Ind AS 110
3. Overview of key relaxations for private companies from certain provisions of the Companies Act, 2013 (2013 Act)

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Overview of Ind AS 110, *Consolidated Financial Statements* and Ind AS 27, *Separate Financial Statements*

Introduction

Step 1: Understand the investee

Step 2: Assess power over relevant activities

Step 3: Assess exposure to variability of returns

Step 4: Assess linkage

Continuous assessment

Separate financial statements

The new control model

To have power, it is necessary for an investor to have existing rights that give it current ability to direct activities that significantly affect an investee's returns (i.e. the relevant activities).

Control assessed on a continuous basis

Under the current guidance in AS 21, *control* is defined as:

(a) the ownership, directly or indirectly through subsidiary(ies), of more than one-half of the voting power of an enterprise, or

(b) control of the composition of the board of directors in the case of a company or of the composition of the corresponding governing body in case of any other enterprise so as to obtain economic benefits from its activities.

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Step 1: Understand the investee

Relevant activities = activities that significantly affect an investee's returns

Conventional operating companies, for example	More likely to consider establishment of operating and capital decisions (e.g. budgets) and appointing, remunerating and terminating key management personnel or services provided
Limited purpose vehicles	More in-depth analysis may be required

Consider purpose and design of an investee and other factors – e.g. factors that determine profit margin, revenue and value of the investee, etc.

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Step 2: Assess power over relevant activities

Gating question

Are voting rights relevant in assessing whether an investor has power over an investee?

Investee controlled by means of voting rights (e.g. conventional operating company)

Investee designed so that voting rights not relevant (e.g. securitisation vehicle)

Power over relevant activities

Voting rights are relevant		Rights other than voting rights are relevant
Majority of voting rights	**Less than a majority**	Consider
Consider	Consider	▪ Purpose and design ▪ Evidence of practical ability to direct ▪ Special relationships ▪ Exposure to variability of returns
▪ Rights held by others (substantive or protective)	▪ Agreements with other vote holders and other contractual agreements ▪ Potential voting rights ▪ De facto power	

Consider only substantive rights

Substantive voting rights

Rights exercisable **when decisions about the relevant activities** of an investee **need to be made**…

…and holder has a **practical ability to exercise** the rights

Factors to consider:

Are there barriers that prevent a holder from exercising the rights?

Do several parties need to agree for the rights to become exercisable or operational?

Would a party holding the rights benefit from their exercise?

Substantive vs Protective rights

Protective rights

- Fundamental changes in activities of an investee or rights that apply only in exceptional circumstances
- Cannot give a holder power or prevent other parties from having power
- Not all rights contingent on future events are protective

Protective rights that become exercisable when certain events or conditions arise may require a reassessment of control

De facto power

Investor with dominant (but not majority) shareholding may have power to direct relevant activities of an investee

- The smaller the size of an investor's holding of voting rights; and
- lesser the dispersion of the holding of other vote holders…
- …greater the need for additional analysis.

Additional factors to consider:
Voting patterns at previous shareholders' meetings
Evidence of practical ability to direct relevant activities
Indications of special relationships with investee
Whether an investor has large exposure to variability of returns

Some scenarios are highly judgemental

Voting rights not relevant (Structured entities)

Purpose and design of an investee

and

- **Evidence of practical ability to direct relevant activities (greatest weight)**
- **Indication of special relationship with investee**
- **Whether an investor has large exposure to variability in returns**

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Step 3: Assess exposure to variability of returns

Analyse whether an investor is exposed to (has rights to) variable returns from its involvement with an investee

Sources of returns (positive and/or negative) include:
Dividends, interests from debt secutiries and changes in value of an investee
Remuneration for servicing an investee's assets and liabilities, fees and exposure to loss from providing credit or liquidity support
Tax benefits
Residual interests in the investee's assets and liabilities on liquidation
Economies of scale, cost savings or other synergies

Maybe more complex and time-consuming when an investor does not hold equity or debt interests

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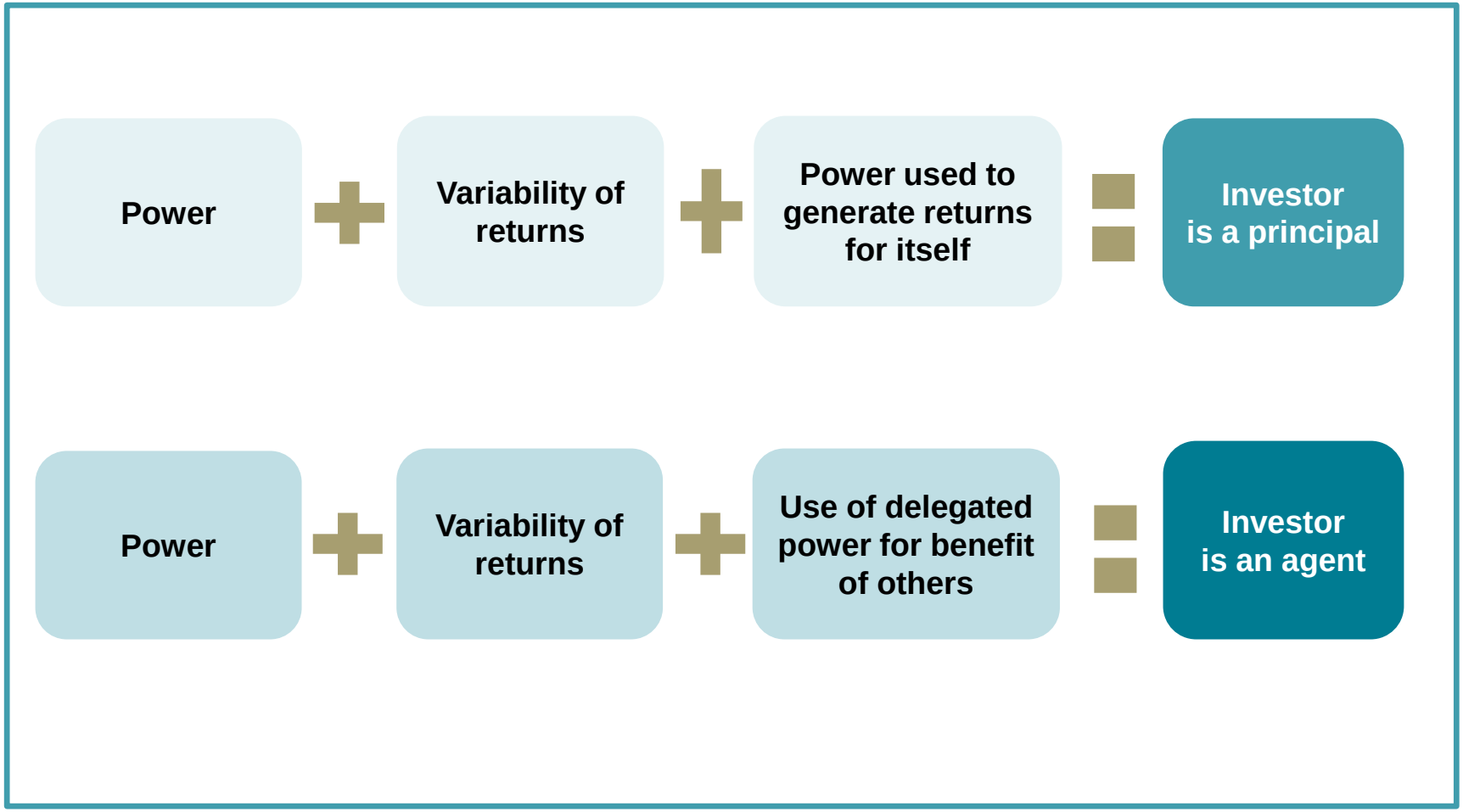
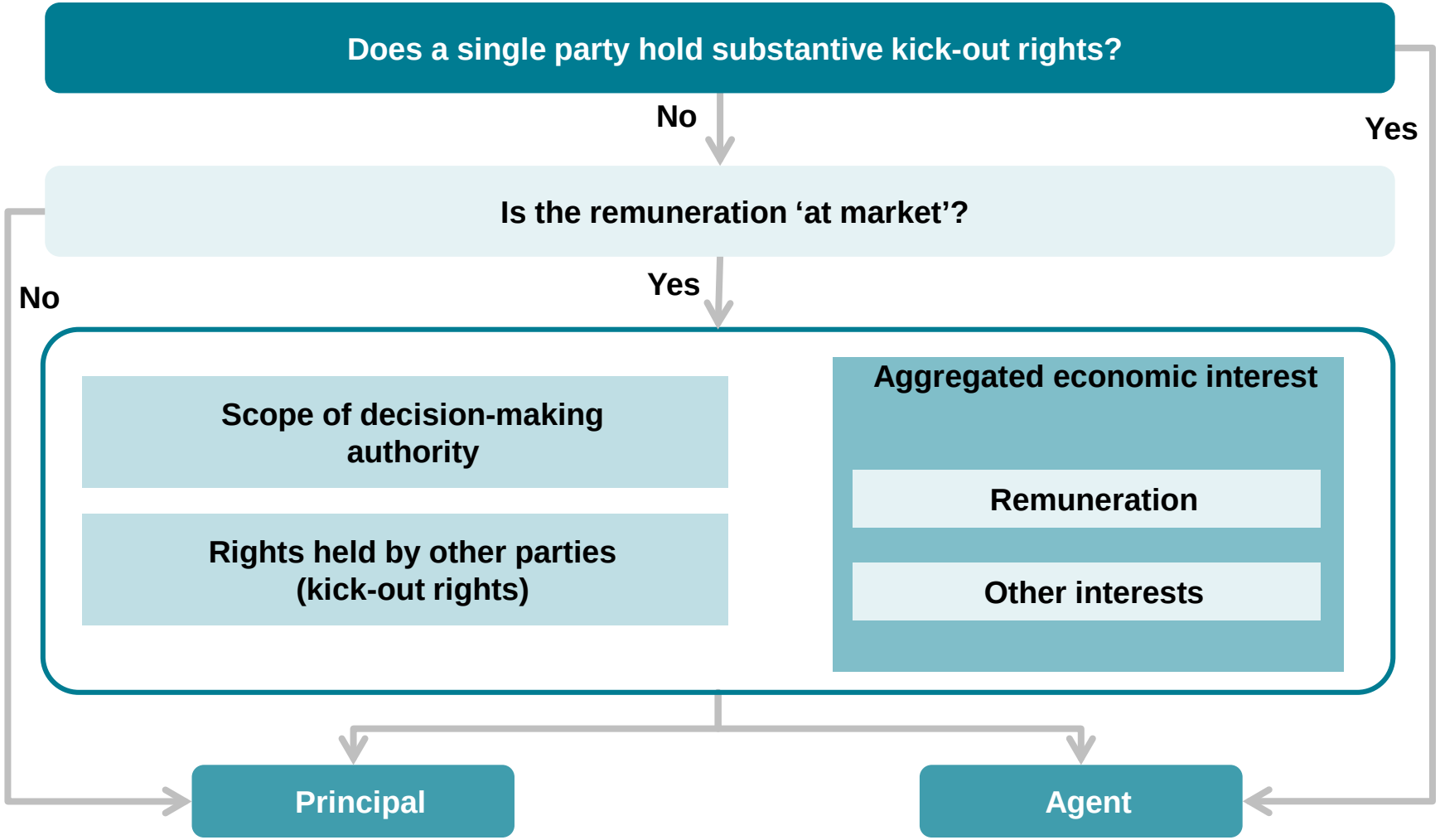


Factors to determine linkage



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Continuous assessment

An investor reassess whether it controls an investee, if facts and circumstances indicate that there are changes to one or more of the elements of control.

Understand the investee	Power	Variability of returns	Link between power and variability
Purpose and design of relevant activities	Substantive rights and how relevant activities are directed	Exposure of parties to variability of returns of an investee	Overall relationship between a principal and an agent

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Separate financial statements

Separate financial statements

- Separate financial statements are prepared in addition to the consolidated financial statements

- Investments in subsidiaries, jointly ventures and associates are accounted for at either:
  - at cost, or
  - in accordance with Ind AS 109

- If a parent is required to measure its investment in a subsidiary at fair value through profit and loss (FVTPL) i.e. in case of investment entities – then it shall account of such investments on the same basis in separate financial statements as well

- If an entity elects to measure its investment in associate or joint venture (as per Ind AS 28, *Investments in Associates and Joint Ventures*) at FVTPL (in accordance with Ind AS 109) - then it shall account of such investments on the same basis in separate financial statements as well

- Dividend from a subsidiary, associate or joint venture should be recognised in the statement of profit and loss when its right to receive the dividend is established.

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3. Overview of key relaxations for private companies from certain provisions of the Companies Act, 2013 (2013 Act)

Key differences between AS 21 and Ind AS 110

Mandatory consolidation	
Under AS 21, presentation of the consolidated financial statements is not mandatory for all companies. Listed companies are required to present consolidated financial statements.	Ind AS 110 requires mandatory preparation of consolidated financial statements by all companies, which have subsidiaries.

Change in definition of control	
Control is assessed based on ownership of more than one-half of the voting power or control of the composition of the Board of Directors (BOD).	Ind AS 110 introduces a new definition of control and a single control model as per which an investor controls an investee when the investor is exposed, or has rights, to variable returns from its involvement with the investee, and has the ability to affect those returns through its power over the investee. The concept of control is wider and requires consideration of veto rights with minority shareholders, structured entities, potential voting rights and de facto control.

Key differences between AS 21 and Ind AS 110

Dilution of parent's ownership interest	
If a parent dilutes its ownership interest in a subsidiary through a sale transaction, the difference between the sale price and the proportionate carrying value of the parent's ownership interest in the subsidiary, is recorded in the profit and loss account. The balance unsold ownership interest continues to be recorded at its original cost.	Under Ind AS, changes in parent's ownership interest in a subsidiary that do not result in a loss of control are accounted for as equity transactions (transactions between shareholders). Accordingly, if a parent sells a portion of the shares in a subsidiary, but there is no loss of control; no gain or loss is recognised in the consolidated statement of profit and loss. However, if there is loss of control, realised gains or losses are recognised in the statement of profit and loss. Further, in such cases, any retained investment is recognised at fair value, with the differential being recognised in the statement of profit and loss.

Key differences between AS 21 and Ind AS 110

Minority interest/Non-controlling interest	
▪ Minority interest is measured at proportionate share in the book values of the net assets of the company	▪ Under Ind AS, the non-controlling interest is measured on the acquisition date at either its fair value or proportionate share of the fair value of the acquired company's identifiable net assets
▪ In case the losses attributable to minority interest in a subsidiary exceed the minority interest in the equity of the subsidiary, such excess and further losses are adjusted against the parent's share, except where the minority has a binding obligation to make good such losses	▪ Under Ind AS, losses relating to the subsidiary are attributed to the non-controlling interest even if it results in a negative balance of the non-controlling interest
▪ Minority interest is presented in the consolidated balance sheet separately from liabilities and equity of the parent's shareholders.	▪ Non-controlling interests should be presented in the consolidated balance sheet within equity separately from parent's shareholders' equity.

Key differences between AS 21 and Ind AS 110

Mandatory use of uniform accounting policies	
In case of impracticability in the use of uniform accounting policies, disclosure of the fact together with the proportions of the items in the consolidated financial statements to which different accounting policies has been applied is required.	When preparing consolidated financial statements, an entity must use uniform accounting policies for reporting like transactions and other events in similar circumstances.

Difference between reporting dates	
A difference of six months between the reporting dates of a parent and a subsidiary is permitted.	The length of the difference in the reporting dates of the parent and the subsidiary should not be more than three months.

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Overview of key relaxations for private companies from certain provisions of the 2013 Act

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Sections/sub-sections that *would not apply* to any private company

Current requirements of the 2013 Act

- **Related party transactions** - Section 2(76)(viii) provides definition of a 'related party'. Section 188 requires that specified transactions with related parties that are not in the ordinary course of business and which are not at an arm's length would require consent of the Board of Directors of the company.

  Further, second proviso to Section 188(1) restricts a member to vote on a special resolution, or approve any contract or arrangement entered into by a company, if such a member is a related party.

- **Resolutions and agreements to be filed** - Section 117 pertains to resolutions and agreements to be filed with the Registrar of Companies (ROC). Section 179(3) requires these resolutions to be passed by the Board. For example, to borrow monies, invest the funds of the company, etc.

Key relaxations for private companies

- The MCA has modified Section 2(76)(viii) and made the following transactions outside the scope of the related party transactions under Section 188:
  - Any company which is a holding, subsidiary or an associate company of such company, or
  - Any company which is a subsidiary of a holding company to which it is also a subsidiary.
- The second proviso to Section 188(1) will not apply to private companies.
- Private companies are no longer required to file with the ROC resolutions passed by the Board which are covered in Section 179(3) of the 2013 Act.

Overview of key relaxations for private companies from certain provisions of the 2013 Act

Sections/sub-sections that *would not apply* to certain class of private companies

- **Section 160** relates to right of persons other than retiring directors to stand for directorship.
- **Section 162** deals with the manner of appointing two or more persons as directors of a company by a single resolution.
- **Section 180** deals with the restrictions on the powers of the Board.
- **Section 196(4) and (5)** relating to appointment and remuneration of managerial personnel.

Overview of key relaxations for private companies from certain provisions of the 2013 Act

Sections/sub-sections that *would apply* to certain class of private companies

Current requirements of the 2013 Act	Key relaxations for private companies
▪ **Loans to directors, etc. -** Section 185 deals with loans to directors and companies in which directors are interested.	▪ Section 185 will not apply to private companies provided that: - no other body corporate has invested in its share capital - which have borrowings from banks or financial institutions or any bodies corporate is less than twice of their paid-up share capital or INR50 crore, whichever is lower, and - such a company has not defaulted in repayment of such borrowings subsisting at the time of making transactions under this Section.

Links to previous recordings of Voices on Reporting

Voices on Reporting

Month	Topics	Link
April 2014	▪ Companies Act – Implementation questions ▪ SEBI corporate governance norms	Click here
May 2014	▪ Companies Act - Matters for first board and general meetings ▪ ICAI's road map for adoption of Ind AS	Click here
June 2014	▪ Companies Act, 2013 – clarifications issued by the Ministry of Corporate Affairs (MCA)	Click here
July 2014	▪ Tax accounting standards – implementation challenges	Click here
August 2014	▪ Related party transactions – the Companies Act, 2013	Click here
September 2014	▪ Recent amendments in tax audit forms ▪ Key amendments to Clause 49 of the Equity Listing Agreement	Click here
November 2014	▪ Exposure draft on Ind AS 101, *First time adoption of Indian Accounting Standards* ▪ Probable benefits and challenges of Ind AS conversion	Click here
January 2015	▪ Ind AS implementation road map ▪ Revised drafts on Income Computation and Disclosure Standards (ICDS)	Click here

Links to previous recordings of Voices on Reporting

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Month	Topics	Link
February 2015	▪ Overview of Income Computation and Disclosure Standards (ICDS) ▪ Significant impact areas of ICDS ▪ Next steps for ICDS implementation	Click here
March 2015	▪ Overview of Section 143(12) of the Companies Act, 2013 ▪ Persons covered for reporting under Section 143(12) of the Companies Act, 2013 ▪ Reporting on frauds in various scenarios	Click here
April 2015	▪ Overview of key changes and implementation challenges for companies that adopt ICDS from this year ▪ Overview of the financial reporting and regulatory developments introduced under the Indian GAAP during the year ended 31 March 2015	Click here
May 2015	▪ Salient features of Ind AS 16, *Property, Plant and Equipment* and Ind AS 38, *Intangible Assets* ▪ Key differences between AS 10, AS 26, Ind AS 16, Ind AS 38 ▪ Key aspects of application guide issued by the Institute of Chartered Accountants of India (ICAI)	Click here
June 2015	▪ Overview of Ind AS 103, *Business Combinations* ▪ Key differences between AS 14 and Ind AS 103 ▪ Overview of key amendments introduced by the Companies (Amendment) Act, 2015	Click here

Q&A

KPMG in India's IFRS Institute – Re-launched

KPMG in India is pleased to re-launch IFRS Institute - a web-based platform, which seeks to act as a wide-ranging site for information and updates on IFRS implementation in India.

The website provides information and resources to help board and audit committee members, executives, management, stakeholders and government representatives gain insight and access to thought leadership publications on the evolving global financial reporting framework.

In addition to proprietary KPMG content, the website provides links to several other sources of information related to IFRS and its implementation. The site can be accessed by all interested parties at no cost. Additionally, the site provides the facility to register as a member by providing certain minimal information.

To download KPMG content, become registered members of the website by following few easy steps.
https://www.in.kpmg.com/IFRS

You can reach us for feedback and questions at
in-fmkpmgifrsinst@kpmg.com

Sources

1. Indian Accounting Standard (Ind AS) 110, *Consolidated Financial Statements* issued by the Ministry of Corporate Affairs (MCA)
2. Indian Accounting Standard (Ind AS) 27, *Separate Financial Statements* issued by the Ministry of Corporate Affairs (MCA)
3. Accounting Standard (AS) 21, *Consolidated Financial Statements* issued by the Institute of Chartered Accountants of India (ICAI)
4. Indian Accounting Standard (Ind AS) 101, *First-time Adoption of Indian Accounting Standards* issued by the Ministry of Corporate Affairs (MCA)
5. KPMG's publication: First Impressions - Consolidated Financial Statements- IFRS 10 (May 2011)
6. KPMG's IFRS Handbook, First-time adoption of IFRS
7. KPMG's Insights into IFRS, 11th edition 2014-15
8. KPMG's publication: Transition to Ind AS - Practical Insights
9. KPMG's IFRS Notes: IFRS Convergence - a reality now! MCA notifies Ind AS standards and implementation road map dated 23 February 2015

Introducing IFRS Notes

Issue 2015/02

The IASB issues a formal proposal to defer the effective date of the new revenue standard

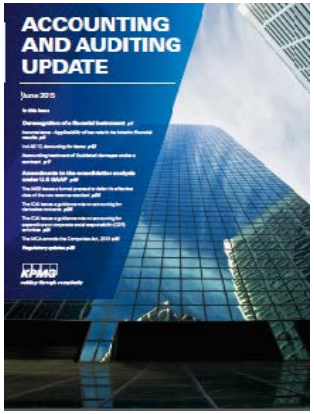
21 May 2015

On 19 May 2015, the IASB published an ED of proposed amendments to IFRS 15 to change the effective date of IFRS 15. It proposes that IFRS 15 would apply for annual reporting periods beginning on or after 1 January 2018. Earlier application would continue to be permitted. Entities would also continue to be permitted to choose between applying the standard either retrospectively to each prior reporting period presented or retrospectively with the cumulative effect of initially applying the standard recognised at the date of initial application.

The IASB also received a number of unsolicited comment letters from stakeholders, e.g. telecommunication and software industries, supporting a deferral of the effective date of IFRS 15. In their view, a one-year deferral would improve the quality of implementation, particularly in the light of the availability (or lack thereof) of information technology systems. Therefore, the IASB holds a view that a one-year deferral would be sufficient in terms of providing additional time to implement IFRS 15.

Topics discussed in AAU and First Notes

Accounting and Auditing update



June 2015

- Derecognition of a financial instrument
- Income Taxes- Applicability of tax rate in the interim financial results
  Ind AS 17, *Accounting for leases*
- Accounting treatment of liquidated damages under a contract
- Consolidation - Amendment to the consolidated analysis
- The IASB issues a formal proposal to defer the effective date of the new revenue standard
- The ICAI issues a guidance note on accounting for derivative contracts
- The ICAI issues a guidance note on accounting for expenditure on corporate social responsibility (CSR) activities
- Regulatory updates

First Notes

The MCA extends the last date for filing of annual return and financial statements forms

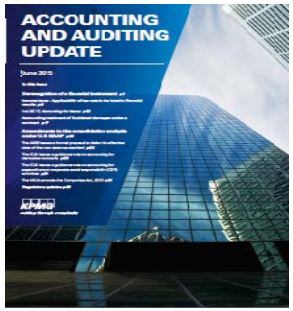
14 July 2015

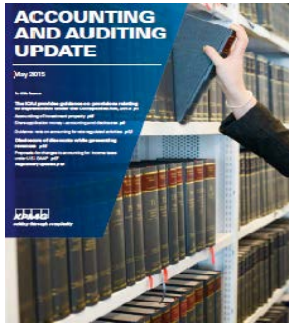
The Ministry of Corporate Affairs has issued a general circular dated 13 July 2015 where it has clarified the following:

- **By 30 September 2015**, the electronic version of the Forms AOC-4, AOC-4 XBRL and MGT-7 will be available for filing.
- **By October 2015**, a separate form for filing of CFS 'AOC-4 CFS' will be made available.
- **Till 31 October 2015**, the Forms AOC-4, AOC-4 XBRL and MGT-7 can be filed with the ROC without payment of additional fees.
- **Till 30 November 2015**, companies to which XBRL is not applicable but are required to file CFS would be able to do so in a separate form for CFS 'AOC-4 CFS' without payment of additional fees.

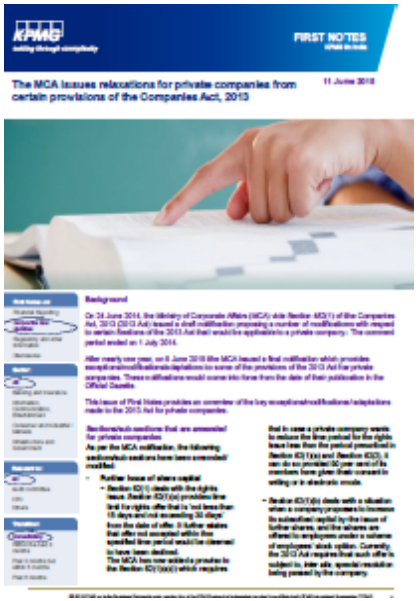
Others

Missed an issue of Accounting and Auditing Update?





Missed an issue of First Notes?



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Coming up next

July 2015

New issue of:

- **Accounting and Auditing Update**
- **First Notes**
- **IFRS Notes**

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