MCA notified amendments to certain Ind AS

10 May 2019

First Notes on

Financial reporting

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Disclosures

Sector

All

Banking and insurance

Information, communication, entertainment

Consumer and industrial markets

Infrastructure and government

Relevant to

All

Audit committee

CFO

Others

Transition

Immediately

Within the next three months

Post three months but within six months

Post six months

Forthcoming requirement

Introduction

Ind AS are largely converged with International Financial Reporting Standards (IFRS) issued by the International Accounting Standards Board (IASB).

The IASB along with the IFRS Interpretation Committee (IFRIC) issue amendments to IFRS as part of the annual improvement process or as specific amendments. Recently, IASB and IFRIC have issued the following amendments and interpretations:

Standard	IFRS amendment issued	Description
	Amendments	
IAS 19, *Employee Benefits*	February 2018	The amendment clarifies the accounting for defined benefit plans on plan amendment, curtailment and settlement.
IAS 28, *Investment in Associates and Joint Ventures*	October 2017	The amendment clarifies the accounting for the share of losses of an associate or joint venture after the equity interest has been reduced to nil.
IFRS 9, *Financial Instruments*	October 2017	The amendments enable entities to measure certain financial assets with prepayment features that may yield a negative compensation on prepayment.
	Annual improvements to IFRS (2015-2017 cycle)	
IFRS 3, *Business Combinations and* IFRS 11, *Joint Arrangements*	December 2017	Additional guidance was provided on acquisition accounting, where an entity obtained control of a joint operation (IFRS 3), or where a participant in a joint operation not having joint control, obtained joint control over the same (IFRS 11).
IAS 12, *Income Taxes*	December 2017	The amendment clarifies the accounting for income tax consequences on distribution of profits.

Standard	Amendment issued in	Description
	Annual improvements to IFRS (2015-2017 cycle) (cont.)	
IAS 23, *Borrowing Costs*	December 2017	The amendment clarifies the borrowing costs to be considered for capitalisation.
	Interpretations	
IFRIC 23, *Uncertainty over Income Tax Treatments*	June 2017	The interpretation provides clarification on the accounting for income taxes, when there is uncertainty over income tax treatments.

In order to keep Ind AS converged with IFRS, MCA has notified above amendments to Ind AS on 30 March 2019.

This issue of First Notes provides an overview of the amendments notified by MCA.

Overview of the amendments

Amendment to Ind AS 19, *Employee Benefits*

The proposed amendments to Ind AS 19 clarify the impact of plan amendments, curtailments and settlements on the following:

- **Current service cost and net interest on the net defined benefit liability (asset)**

  Currently, Ind AS 19 requires entities to remeasure the net defined benefit liability (asset) on plan amendment, curtailment or settlement, using the updated actuarial assumptions and accordingly determine the past service cost. However, the current service cost and net interest are calculated on the basis of assumptions at the beginning of the annual reporting period.

  In order to provide useful information to the users and enhance the understandability of financial statements, the change to the standard requires that on amendment, curtailment or settlement of a defined benefit plan, entities should:

  – Update actuarial assumptions to those used to remeasure the net defined benefit liability (asset), and

  – Use the updated assumptions and the revised net defined benefit liability (asset) to determine the current service cost and net interest for the remainder of the annual reporting period (post the plan amendment, curtailment or settlement).

- **Effect on asset ceiling requirements**

  Currently, the net defined benefit assets are measured at lower of the surplus[1] and the asset ceiling[2]. The accounting for a plan amendment, curtailment or settlement could reduce or eliminate a surplus, which could cause the effect of the asset ceiling to change.

  The amendment clarifies that entities should disregard the asset ceiling when determining the past service cost on plan amendment or curtailment, or the gain or loss on settlement of the plan, and recognise the past service cost or the gain or loss in the statement of profit and loss. Subsequently, the effect of the asset ceiling should be recognised in other comprehensive income.

Effective date and transition

The amendment is applicable for plan amendments, curtailments or settlements occurring on or after 1 April 2019.

Amendments to Ind AS 28, *Investment in Associates and Joint Ventures*

Long-term interests in associates and joint ventures

An entity's net investment in its associate or joint venture includes investment in ordinary shares, other interests that are accounted using the equity method, and other long-term interests, such as preference shares and long term receivables or loans, the settlement of which is neither planned, nor likely to occur in the foreseeable future. These long-term interests are not accounted for in accordance with Ind AS 28, instead, they are governed by the principles of Ind AS 109.

As per para 10 of Ind AS 28, the carrying amount of an entity's investment in its associate and joint venture increases or decreases (as per equity method) to recognise the entity's share of profit or loss of its investee associate and joint venture. Paragraph 38 of Ind AS 28 further states that the losses that exceed the entity's investment in ordinary shares are applied to other components of the entity's interest in the associate or joint venture in the reverse order of their superiority.

[1] Surplus is the excess of the fair value of plan assets over the present value of the defined benefit obligation.

[2] Asset ceiling is the present value of economic benefits available in the form of refunds from the plan or reductions in future contributions to the plan.

In this context, the amendments to Ind AS 28 clarify that the accounting for losses allocated to long-term interests would involve the dual application of Ind AS 28 and Ind AS 109. The annual sequence in which both standards are to be applied can be explained in a three step process:

1 **Apply Ind AS 109 independently**

Apply Ind AS 109 (such as impairment, fair value adjustments, etc.) ignoring any adjustments to carrying amount of long-term interests under Ind AS 28 (such as allocation of losses, impairment, etc.)

2 **True-up past allocations**

If necessary, prior years' Ind AS 28 loss allocation is trued up in the current year, because Ind AS 109 carrying value may have changed. This may involve recognising more prior year's losses, reversing these losses or re-allocating them between different long-term interests.

3 **Book current year equity share**

Any current year Ind AS 28 losses are allocated to the extent that the remaining long-term interest balance allows. Any current year Ind AS 28 profits reverse any unrecognised prior years' losses and then allocations are made against long-term interests.

Source: KPMG in India's analysis, 2019 read with Long-term interests in associates and joint ventures, KPMG IFRG Ltd.'s publication, 17 October 2017

Effective date and transition

These amendments are applicable retrospectively[3] from 1 April 2019.

The MCA has provided the following transitional provisions:

- Where entities apply the amendment when they first apply Ind AS 109, then they would benefit from applying the transition requirements in Ind AS 109
- Where entities apply the amendments after they first apply Ind AS 109, then they are permitted to apply transition requirements similar to Ind AS 109 with respect to provisions of long-term interests, and
- Where entities choose not to restate prior periods at the date of initial application of the amendments, they should recognise in the opening retained earnings the difference between the carrying amount of the long-term interest prior to the amendment, and the long-term interest post the amendment.

Amendments to Ind AS 109, *Financial Instruments*

Prepayment features with negative compensation

While determining the classification and measurement of financial assets, Ind AS 109 requires entities to consider the business model in which they are held and the contractual cash flow characteristics of the asset. Based on these two factors, entities may classify the financial assets as subsequently measured at amortised cost, Fair Value through Other Comprehensive Income (FVOCI) or Fair Value through Profit or Loss (FVTPL).

A financial asset would be classified and measured at amortised cost or at FVOCI if its contractual cash flows are solely in the nature of principal and interest on the principal amount outstanding (SPPI criterion).

Paragraph B4.1.10 read with paragraph B4.1.11(b) of Ind AS 109 states that a prepayment option in a financial asset meets the SPPI criterion if the prepayment amount substantially represents the unpaid amount of principal and interest, which may include reasonable additional compensation for early termination of the contract.

In a situation where a financial asset that had a prepayment option, which permitted the borrower to prepay the financial asset at an amount that reflected the remaining contractual cash flows of the asset, discounted at a market interest rate. This could result in the other party being forced to accept a negative compensation.

[3] In accordance with Ind AS 8, *Accounting Policies, Changes in Accounting Estimates and Errors.*

[4] Earlier, paragraph B4.1.11b had a requirement for the prepayment amount to represent unpaid amount of principal and interest, which may include reasonable additional compensation. The amendment has now removed the word 'additional' so that negative compensation may be regarded as 'reasonable compensation' irrespective of the cause of the early termination.

[5] Where amount received would be lower than the unpaid amount of principal and interest, when the market interest rate was higher than the effective interest rate of the instrument.

Such an asset would not have cash flows that meet the SPPI criterion (because of the negative compensation), hence the asset would be classified and measured at FVTPL. This would result in an inappropriate measurement, where amortised cost provided useful information.

In view of this, the amendment carries an exception to the classification and measurement requirements with respect to the SPPI criterion for financial assets that:

- Have a prepayment feature which results in a negative compensation
- Apart from the prepayment feature, other features of the financial asset would have contractual cash flows which would meet the SPPI criterion, and
- The fair value of the prepayment feature is insignificant when the entity initially recognises the financial asset. If this is impracticable to assess based on facts and circumstances that existed on initial recognition of the asset, then the exception would not be available.

Such financial assets could be measured at amortised cost or at FVOCI based on the business model within which they are held.

Effective date and transition

These amendments are applicable retrospectively from 1 April 2019.

As a consequence of amendments to Ind AS 109 and the proposed Ind AS 117, *Insurance Contracts*, certain transitional provisions have been inserted in Ind AS 109. The transitional provisions should be considered when first applying the amendments, or when specifically mentioned. These pertain to the following:

Transitional provisions on first-time application of amendments:

- Where the entity applies these amendments when it first applies Ind AS 109, then relevant provisions of Ind AS 101, *First-time Adoption of Indian Accounting Standards* would apply
- Where the entity applies these amendments after it first applies Ind AS 109, it would apply other transitional requirements (as given below)
- Entities should designate financial assets and financial liabilities at FVTPL/revoke such designation retrospectively, based on whether the facts and circumstances that exist on the date of initial application of the amendment satisfy the conditions prescribed in the standard.
- Entities may restate the prior periods without the use of hindsight, provided, the restated financial statements reflect all the requirements in this standard. Where the prior periods are not restated, entities should recognise any difference between the previous carrying amount and the carrying amount at the beginning of the annual reporting period that includes the date of initial application of these amendments in the opening retained earnings.
- In the reporting period that includes the date of initial application, the entity should disclose the following information for each class of financial assets and financial liabilities that were affected by these amendments:
  - The previous measurement category and carrying amount determined immediately before applying these amendments
  - The new measurement category and carrying amounts determined after applying these amendments, and
  - The carrying amounts of financial assets and financial liabilities in the balance sheet that were previously designated as measured at FVTPL, but are no longer so designated, and the reasons for any designation or revocation of previous designation.

Transitional provisions on classification and measurement

- **Application**: Entities should apply this standard retrospectively in accordance with Ind AS 8, except when specifically mentioned. The standard would not be applicable to items that have already been derecognised at the date of initial application
- **Business model:** Business model of financial assets would be assessed based on facts and circumstances existing on the date of initial application of the amendments[6], and be applied retrospectively
- **Impracticability provision**: The amendment inserted certain transitional provisions with respect to determining the contractual cash flow characteristics of financial assets or the gross carrying amount/amortised cost of financial assets/financial liabilities respectively. These are:
  - While determining the contractual cash flow characteristics of financial assets, where it is impracticable to assess either the modified time value of money element[7] or the fair value of the prepayment features on the basis of facts and circumstances that existed on initial recognition of the financial asset, the cash flow characteristics would be assessed without taking into account these features

[6] For entities applying these amendments after they have first applied Ind AS 109, reference to date of initial application would be read as referring to beginning of reporting period in which an entity first applied these amendments.

[7] Time value of money is the element of interest that provides consideration for passage of time.

- o While determining the contractual cash flow characteristics of financial assets, where it is impracticable to assess either the modified time value of money element[9] or the fair value of the prepayment features on the basis of facts and circumstances that existed on initial recognition of the financial asset, the cash flow characteristics would be assessed without taking into account these features
- o If the entity finds it impracticable to apply the effective interest method retrospectively, it may consider the fair value of the financial asset or the financial liability on the date of initial application of the amendments as its new gross carrying amount or new amortised cost respectively. If the entity restates prior periods, the fair value at the end of each comparative period can be presented as the gross carrying amount/amortised cost on that date

- **Designation of instruments**: On the basis of facts and circumstances that exist on the date of initial application, entities may designate a financial asset as measured at FVTPL, designate investments in equity instruments at FVOCI or designate a financial liability as measured at FVTPL as per provisions in Ind AS 109, or revoke such designations on a retrospective basis.
- **Change in fair value of liabilities designated at FVTPL**: On the date of initial application, the entity should determine whether the treatment of change in fair value of liabilities designated at FVTPL would create or enlarge an accounting mismatch in profit or loss on the basis of facts and circumstances on date of initial application, and make changes (if any) retrospectively.

Amendments to Ind AS 12, *Income Taxes*

A. Insertion of Appendix C, Uncertainty over Income Tax Treatments

Background

Paragraph 12 of Ind AS 12 provides guidance on recognition of income tax assets and liabilities. It requires entities to recognise a current tax liability for taxes pertaining to the current and prior periods, to the extent they are unpaid and to recognise an asset if the taxes paid in respect of the current and prior periods exceed the amounts due for those periods, to the extent of such excess amounts paid. However, sometimes it is unclear on how tax law applies to a particular transaction or circumstance. Since interpreting areas of uncertainty in tax law can be complex, entities have adopted different approaches for recognising tax liabilities and assets. This has resulted in diversity in practice for the recognition and measurement of a tax liability or asset in the financial statements of entities.

Appendix C to Ind AS 12 (Appendix C) seeks to bring clarity to the accounting for uncertainties on income tax treatments that have yet to be accepted by tax authorities, and to reflect it in the measurement of current and deferred taxes.

Key highlights of Appendix C

Assumption

Entities applying Appendix C, need to consider the following assumptions:

- The taxation authorities have the right to examine the amounts reported to them
- The taxation authorities will examine the amounts reported to them; and
- The taxation authorities will have full knowledge of all relevant information in assessing a proposed tax treatment.

Consideration of uncertain tax treatments individually/collectively

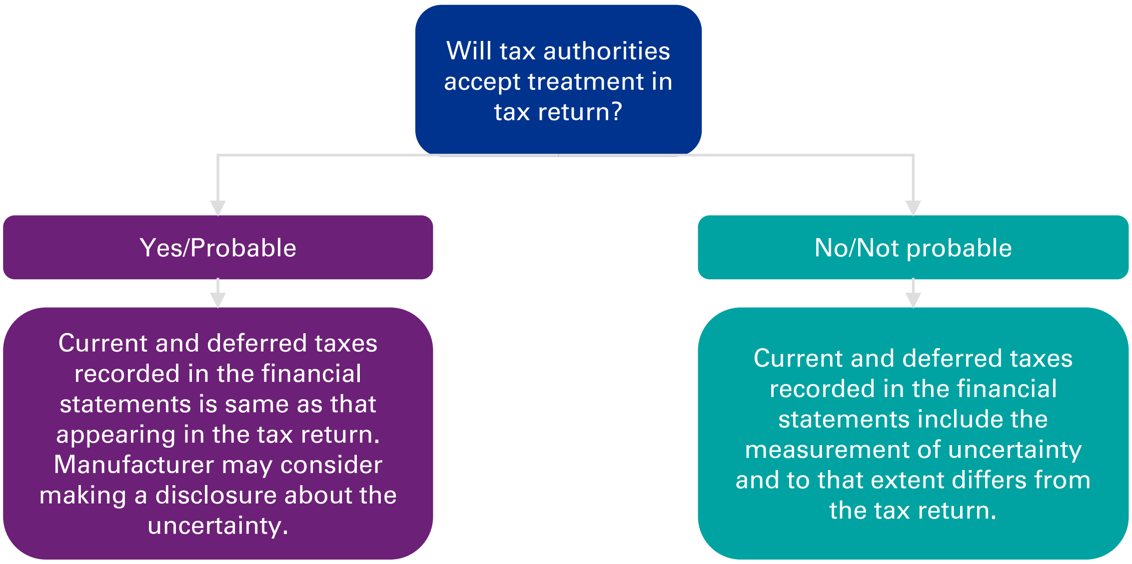
Appendix C requires entities to first determine whether they should consider uncertain tax treatments individually or collectively, with other uncertain tax treatments, depending on which approach would provide a better prediction of the resolution of the uncertainty.

The key test

As per Appendix C, the key test is whether it is probable that the taxation authority would accept the tax treatment used or planned to be used by the entity in its income tax filings. If yes, then the amount of taxes recognised in the financial statement would be consistent with the entity's income tax filings. Otherwise, the effect of uncertainty should be estimated and reflected in the financial statements. This would require the exercise of judgement by the entity. This is further explained below with the help of an example.

Consider a manufacturer that engages a consultant to improve the efficiency of its production process. The manufacturer believes that deducting the full expenses from profit up-front would be consistent with the principles of its local tax law, and therefore applies that treatment in its tax return. However, the manufacturer is not sure whether the tax authorities will agree.

To determine the current tax liability to be recognised by the manufacturer in its financial statements, it needs to consider whether it is probable that the taxation authority will accept the treatment in the tax return. This can be evaluated with the help of a diagram on the next page.



Source: KPMG in India's analysis, 2019 read with Income tax exposures: IFRIC 23 clarifies the accounting treatment, KPMG IFRG Ltd.'s publication, June 2017

Recognition and measurement of uncertainty

The uncertainty is reflected using the measure that provides the better prediction of the resolution of the uncertainty either:

- The most likely amount – being the single most likely amount in a range of possible outcomes; or
- The expected value – the sum of probability-weighted amounts in a range of possible outcomes.

The measurement of uncertainty is reflected in the overall measurement of tax, and no separate provision is required to be made.

Appendix C requires companies to reassess the judgements and estimates applied, and update the amounts in the financial statements, if facts and circumstances change as below:

- As a result of examination or action by tax authorities
- Following changes in tax rules
- When a tax authority's right to challenge a treatment expires
- Any other new facts and circumstances, including adjusting events occurring after the reporting period under Ind AS 10, *Events after the Reporting Period*, that may affect an entity's conclusion about the acceptability of tax treatments.

Accounting impact and disclosures

Depending on their current practice, entities may need to increase their tax liabilities or recognise an asset. The timing of derecognition may also change.

Appendix C does not introduce any new disclosure requirements, but reinforces the need to comply with the meaningful disclosure requirement under Ind AS 1, *Presentation of Financial Statements* and the existing disclosure requirements under Ind AS 12, which include disclosure requirements of:

- Judgements made
- Assumptions and other estimates used; and
- The potential impact of uncertainties that are not reflected.

Effective date and transition

Appendix C is applicable for annual periods beginning on or after 1 April 2019.

On transition, a company may apply the standard retrospectively, by restating the comparatives (i.e. period beginning 1 April 2018), if this is possible without the use of hindsight, or apply it prospectively by adjusting equity on initial application, without adjusting comparatives.[8]

[8] IFRS Notes: IFRIC 23 clarifies the accounting treatment for uncertain income tax treatments, KPMG India's publication dated 13 June 2017.

B. Amendments to Ind AS 101

The notification of Appendix C has inserted consequential amendments to Ind AS 101. These amendments would be applicable to first-time adopters when they apply Appendix C.

The amendment clarifies that when the date of transition to Ind AS is before the date of notification of Appendix C, then a first-time adopter of Ind AS may elect not to reflect the application of Appendix C in the comparative information of the first Ind AS financial statements. Instead, it may recognise the cumulative effect of applying Appendix C as an adjustment to the opening balance of retained earnings at the beginning of the first Ind AS reporting period.

C. Annual improvements

Income tax consequences on distribution of profits

The amendment to Ind AS 12 clarifies that the income tax consequences of distribution of profits (i.e. dividends), including payments on financial instruments classified as equity, should be recognised when a liability to pay dividend is recognised. The income tax consequences should be recognised in profit or loss, other comprehensive income or equity according to where the past transactions or events that generated distributable profits were originally recognised.

Further, by moving the requirement of recognising the income tax consequences from paragraph 52B to paragraph 57A, the amendment clarifies that the requirement for recognition applies to all income tax consequences and not only to the situation where there are different tax rates for distributed and undistributed profits as described in paragraph 52A of Ind AS 12.

Effective date and transition

These amendments are applicable prospectively for annual reporting periods beginning on or after 1 April 2019.

Annual improvements to Ind AS (2018)

Amendments to Ind AS 103, *Business Combinations* and Ind AS 111, *Joint Arrangements*

A new paragraph 42A to Ind AS 103 has been added to clarify that when an entity obtains control of a business that is a joint operation, then the acquirer would remeasure its previously held interest in that business. Such a transaction would be considered as a business combination achieved in stages and accounted for on that basis.

Further, paragraph B33CA has been added to Ind AS 111 to clarify that if a party that participates in a joint operation, but does not have joint control, obtains joint control over the joint operation (which constitutes a business as defined in Ind AS 103), it would not be required to remeasure its previously held interests in the joint operation. The amendment points out that although such a transaction changed the nature of the entity's interest in the joint operation, it did not result in a change in the group boundaries. Consequently, no remeasurement of previously held interests would be required.

Effective date and transition

These amendments are applicable prospectively for business acquisitions (in case of Ind AS 103) or transactions where joint control is obtained (in case of Ind AS 111) where the date of the transaction is on or after the beginning of the first annual reporting period beginning on or after 1 April 2019.

Amendments to Ind AS 23, *Borrowing Costs*

The amendment clarifies that in computing the capitalisation rate for funds borrowed generally, an entity should exclude borrowing costs applicable to borrowings made specifically for obtaining a qualifying asset, only until the asset is ready for its intended use or sale. Borrowing costs related to specific borrowings that remain outstanding after the related qualifying asset is ready for intended use or for sale would subsequently be considered as part of the general borrowing costs of the entity.

Effective date and transition

The amendment is applicable to borrowing costs incurred on or after the beginning of the annual reporting period beginning on or after 1 April 2019.

Our comments

- **Amendment to Ind AS 19:** As per the amendment, the current service cost and net interest on a defined benefit plan is required to be recomputed on a plan amendment, curtailment or settlement. Currently entities are not required to update the calculation of these costs until the year-end. Thus this may result in significant changes in the total personnel cost for the year if an entity undertakes a plan amendment, curtailment or settlement.

- **Amendment to Ind AS 28:** Currently, there has been diversity in practice when accounting for the share of losses of an associate or joint venture after the equity interest has been reduced to nil. The balance share of losses was allocated to other long-term interests, however, the accounting treatment of such long-term interests under Ind AS 109 was unclear. This amendment will promote consistency in practice, but at the same time likely to result in some complexity.

- **Amendment to Ind AS 109:** This amendment may provide relief to entities that are party to contracts that include a prepayment feature with negative compensation. However, the amendment is narrow in its scope and would not extend to compensation based on fair value changes and break costs of related hedges at the time of prepayment.

- **Appendix C to Ind AS 12:** While applying the clarification provided in Appendix C, it would be challenging for entities to estimate the income tax due with respect to tax inspections, when tax authorities examine different types of taxes together and issue a report with a single amount due therein.

  The actual taxes payable (receivable) as finalised by the tax authorities, may differ from the amounts recognised as current tax liabilities (assets) in the financial statements on account of uncertainties on income tax treatment of items or transactions.

  As a result of Appendix C, the effect of uncertainties on income tax treatment of items or transactions should be assessed by the entity. Depending on the probability of the taxation authorities accepting the treatment in the tax return, the entity would either disclose the uncertainty in the financial statements or include an adjustment for the same in the tax provision for that year.

  Appendix C does not specifically address tax assets and liabilities acquired or assumed in a business combination. Ind AS 103, *Business Combinations* requires entities to apply Ind AS 12 to account for deferred tax assets and liabilities acquired or assumed in a business combination, hence the interpretation would apply, when there is uncertainty over income tax treatments that affect deferred taxes.

  Absence of an explicit agreement or disagreement by the taxation authorities on its own is unlikely to represent a change in facts and circumstances, or new information that affects the judgements and estimates made. Accordingly, this has to be assessed in accordance with other available information.

  When the key test of the interpretation would result in the entity recognising tax assets (i.e. based on the probability that the taxation authorities would accept the entity's tax treatment), the entity is not required to demonstrate the 'virtual certainty' of the tax authority accepting the entity's tax treatment in order to recognise such a tax asset.

- **Annual improvements to Ind AS (2018):** The amendments provide clarity on various areas that are a matter of diversity in practice.

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

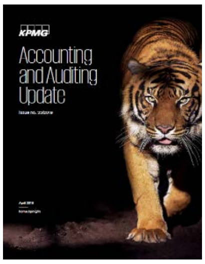
RBI defers implementation of Ind AS for banks till further notice

26 March 2019

Scheduled Commercial Banks (SCBs) excluding Regional Rural Banks (RRBs) were initially required to implement Indian Accounting Standards (Ind AS) from 1 April 2018. However, RBI vide a press release dated 5 April 2018, deferred the implementation of Ind AS by one year i.e. 2019-20 would have been the first year of Ind AS with 2018-19 as the comparative year.

The RBI through a notification dated 22 March 2019, has further deferred the Ind AS implementation till further notice.

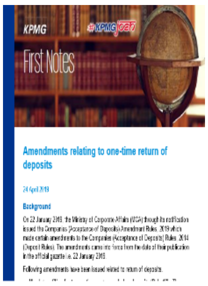
Missed an issue of Accounting and Auditing Update or First Notes



Issue no. 33 – April 2019

The topics covered in this issue are:

- Hedging a foreign currency risk using a forward contract
- Accounting for a loan taken from a shareholder subsequent to restructuring
- Significant developments related to SEC listed companies
- Regulatory updates.



Amendments relating to one-time return of deposits

24 April 2019

On 22 January 2019, the Ministry of Corporate Affairs (MCA) through its notification issued the Companies (Acceptance of Deposits) Amendment Rules, 2019 which made certain amendments to the Companies (Acceptance of Deposits) Rules, 2014 (Deposit Rules).

The MCA through its circular dated 12 April 2019 further amended Rule 16A relating to one-time return for outstanding receipts not considered as deposits.

In this issue of First Notes, we aim to provide an overview of the key amendments relating to one-time return.

Voices on Reporting

KPMG in India is pleased to present Voices on Reporting – a series of knowledge sharing calls to discuss current and emerging issues relating to financial reporting.

Voices on Reporting- annual update publication (for the year ended 31 March 2019) provides a summary of key updates from the Ministry of Corporate Affairs, the Securities and Exchange Board of India and the Institute of Chartered Accountants of India.

The publication can be accessed at KPMG in India website.

Feedback/queries can be sent to aaupdate@kpmg.com

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