Accounting and Auditing Update

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KPMG in India has introduced a revamped series of the Accounting and Auditing Update which covers recent affairs in accounting, financial reporting and the regulatory challenges being faced by diverse sectors in India. Each month’s publication focusses on a different sector. This month, we explore various aspects related to the Media and Entertainment (M&E) sector.

Ind AS is bringing about a paradigm shift in financial reporting which is going to potentially affect many key metrics of performance across various sectors. In this publication, we have highlighted four key areas of impact: revenue recognition, intangible assets such as programme assets and similar rights, acquisitions and business combinations, and consolidation.

The M&E sector has distinct and complex revenue arrangements such as: barter arrangements, arrangements where careful evaluation is required on whether revenue should be recognised at gross amount or net amount, free/discounted advertising and bonus spots, carriage fees, etc. Our articles explain the accounting requirements on these topics under current Indian GAAP and Ind AS.

Additionally, accounting of amortisation of intangible assets (e.g. media rights) is expected to be challenging under Ind AS. Our article on the same explains the implementation of the new requirements.

In the interview section of our publication, we speak to CFOs/finance directors of leading companies from the industry, exploring some of the key accounting, reporting and topical matters relevant to the industry. This month’s issue features interviews with two industry leaders: Mr. Nitin Nadkarni, Chief Financial Officer, Multi Screen Media Private Limited and Mr. Sujit Vaidya, Vice President and Chief Financial Officer, The Walt Disney Company (India) Private Limited. They share their perspectives and experience on a wide range of issues.

The M&E sector faces various direct and indirect tax issues for example: withholding taxes, deductibility of expenses, impact of proposed Goods and Services Tax (GST), service tax, etc. Our article provides an overview on these tax issues.

Finally, our publication also includes our regular round up of regulatory updates. As always, we would be delighted to receive any kind of feedback or inputs on the topics that we have covered.
The recent years have indicated a turnaround for the Media and Entertainment (M&E) sector in India in many ways. The country’s significant consumer market base and increasingly favourable macroeconomic and regulatory environment have prompted several investors and global players to look at the Indian market and secure growth opportunities. For Indian players, tailored content strategies for the audiences (be it global, national or local), and a focus on building the relevant digital and physical touchpoints to enable easier and more open and interactive access could be key success factors going forward. With this, India could be at the cusp of significant growth and earn its place in the global spotlight.

Digital media continues its rapid penetration, with eyeballs that earlier used to be captivated by the TV, print and other traditional media are now shifting base to online channels. The availability of affordable smartphones and tablets has fuelled the ‘second screen’ phenomenon that cannot be ignored by content creators, curators and advertisers alike. The next wave of growth in internet penetration is expected to be driven by the adoption of internet in rural areas, whose first experience with the internet could come through mobile phones.

Advertising on television has seen robust growth over the years, which is primarily driven by the positive shift in the macroeconomic environment, the general election spends, and the emergence of e-commerce as a significant new advertising spender. At the same time, despite the roll-out of digital Set Top Boxes (STBs) as a part of the ongoing Digital Addressable System (DAS), the anticipated improvement in addressability, increase in subscription revenues and further equitable sharing of subscription revenues continues to evade the industry.

The print sector continues to remain a highly fragmented space, at the national and regional level. In recent years, the print industry witnessed a rise in circulation revenues on the back of rising cover prices and subscriptions, aided by low media penetration, population growth and rising income and literacy levels. This growth largely comes from Tier II and Tier III cities with regional language editions outperforming the national editions as well as English dailies.

The film exhibition sector saw several players expanding their footprint; both organically (especially in Tier II and Tier III cities) and through acquisitions. The cable and satellite market also saw correction. Regional films continued to see success, in particular the Tamil and Telugu markets. Going forward, with an increasing number of multiplex screens and better internet penetration and bandwidth, Tier II and Tier III cities may soon hold prime focus for the industry. For TV and digital content producers, original programming for Video On Demand (VoD) and Over The Top (OTT) platforms is emerging as the next big growth driver. Content is likely to be a critical success factor for the platform, hence content deals are increasingly turning exclusive as competition heats up for distinct and quality content.

The radio sector saw the much awaited movement in Phase III auctions, with the government giving its go ahead for partial auctions across 69 cities, where potentially 136 channels are up for grabs. The e-auction commenced on 27 July 2015 and over 32 days, 125 rounds of bidding took place. The total value of sold channels was INR 1,187 crore. However, some key contentious issues of exorbitant reserve prices for the auctions, the 15 per cent limit on the total number of frequencies that an entity may hold, as well as dearth of new frequencies in the profitable A and A+ cities remain. The commencement of Phase III provided the required fillip to the industry which hopes to revive its fortunes with these new developments.

The industry faces a great deal of accounting and regulatory issues arising out of the governing laws, regulations, operational issues, etc. The publication examines some of the key financial, accounting and regulatory issues that are expected to be encountered by the industry in the near future.
Impact of Ind AS on the M&E sector

This article aims to:
- Highlights key differences between the current accounting practices and policies followed by the companies in M&E sector and the consequent requirements under Ind AS.
- Highlights the impacts of requirements under Ind AS.

Ind AS is bringing about a paradigm shift in financial reporting which is going to potentially affect many key metrics of performance. In this article, we have highlighted four key areas of impact: revenue recognition, intangible assets such as program assets and similar rights, acquisitions and business combinations and consolidation. Our article explains the new accounting requirements in these areas and the expected challenges that are likely to be faced by the sector.

Key accounting issues

Revenue recognition

It is expected that Ind AS 115, Revenue from Contracts with Customers may get deferred in line with a shift in timelines for IFRS 15, Revenue from Contracts with Customers, globally. The Institute of Chartered Accountants of India (ICAI) has already issued an Exposure Drafts for Ind AS 18, Revenue, and Ind AS 11, Constructions Contracts, which are likely to replace Ind AS 115. The section below highlights requirements of proposed Ind AS 18 and Ind AS 115.

Free/discounted advertising and bonus spots

Television broadcasters sometimes guarantee their advertising customers certain minimum audience ratings in their target group, failing which the broadcaster may grant reductions on future advertising prices or free advertising time. Under Ind AS 18, since the broadcaster has a constructive obligation to compensate the advertising customer, certain portion of the revenue would be deferred and be recognised subsequently when the free/discounted advertising is utilised; or on the expiry of the maximum period available for utilisation (if the free/discounted advertising is ultimately not utilised by the customer). Under Ind AS 18, revenue could be allocated to components by either using the relative fair value method or the fair value of the undelivered components (residual value method).

Similarly, broadcasters may enter into arrangements for free/bonus spots, bundled with normal paid spots. This arrangement may be documented in one overall agreement or through separate agreements entered contemporaneously. Under Ind AS 18, the total consideration for advertising services would be allocated to the paid and bonus spots based on either their relative fair values or on the basis of the fair value of bonus spots using the residual value method. Revenues allocated to bonus spots would be recognised when such spots are utilised.
Under Ind AS 115, a transaction price would be allocated to each performance obligation on a relative stand-alone selling price basis. The standard describes three estimation methods:

<table>
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<th>Method</th>
<th>Description</th>
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<tr>
<td>Adjusted market approach</td>
<td>Evaluate the market in which the goods or services are sold and estimate the price that the customers might be willing to pay.</td>
</tr>
<tr>
<td>Expected cost plus a margin approach</td>
<td>Forecast the expected costs of satisfying a performance obligation and then add an appropriate margin for that good or service.</td>
</tr>
<tr>
<td>Residual approach (limited cases)</td>
<td>Subtract the sum of the observable stand-alone selling prices of other goods or services promised in the contract from the total transaction price.</td>
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Under Ind AS 115, the residual approach can be applied only if the stand-alone selling price of one or more goods or services is highly variable or uncertain. Therefore, when applying Ind AS 18, entities should choose the relative fair value approach for allocating revenues to various components as it will help with the transition to Ind AS 115.

Currently under Indian GAAP, in practice constructive obligations are generally not recognised and no revenues are allocated to the free/bonus spots. Accordingly, revenues are generally recognised when the paid spots are aired, with no deferral of revenue for free/bonus spots.

**Bundled contracts**

In the M&E sector, there are several types of multiple-element arrangements. For example, the sale of a cable subscription agreement is combined with the provision of the necessary decoder at a discounted price, activation and set-up fees associated with channel subscription and triple-play agreements (where the deliverables are the television, telephone and internet). Similarly, in the publishing industry, publishers may sell a range of information solutions that combine print and online products. While the print product has a fixed edition status at the time of sale, an online product includes regular updates to the information contained in the print product, which is provided over the internet for a certain period of time in the form of a time-limited subscription.

Under Ind AS 18, it may be necessary to segment a single contract into its components (elements), with different revenue allocations for each component. Generally, if separate elements have a stand-alone value to a customer, the allocation of overall revenues to individual elements would be required irrespective of whether all elements are documented in a single contract or in separate concurrent contracts.

Thus, the substance of the arrangement is evaluated to determine whether multiple elements are involved. After identification of separate obligations, revenue is allocated based on either the relative fair values of each component or the residual fair value method. The use of the reverse residual method may not be permitted.

Currently under Indian GAAP, many of the Indian M&E sector account for each deliverable within the overall arrangement based on the form of documentation in the contract and based on the prices stated in the contract. Typically, no separate evaluation of multiple elements existing in a single legal contract is performed. Similarly, a separate fair value for each element within the contract is not determined if separate prices are stated in the contract for each deliverable.

Accordingly, application of Ind AS 18 may result in a deferral of revenue in several cases, where upfront recognition is currently followed. For example, activation fees which may currently be recognised as revenue on the date of installation, may need to be deferred and recognised over a customer relationship period.

Additionally, internal reporting systems (including IT systems), processes and internal controls would need to evolve to determine the separation of multiple elements embedded in a single or concurrently negotiated contract, and for helping ensure the availability of sufficient benchmark data to support the fair value allocation.

Under Ind AS 115, at contract inception, it should be assessed whether the goods or services have been explicitly or implicitly promised in a contract and should identify as a performance obligation each promise to transfer a distinct good or service.

A good or service that is promised in a contract is ‘distinct’ if both of the following criteria are met with:

- **Criterion 1**: The customer can benefit from the good or service either on its own or together with other resources that are ‘readily available’ to the customer.
- **Criterion 2**: The entity’s promise to transfer the good or service to the customer is separately identifiable from other promises in the contract.

The customer can benefit from the good or service if it can be used, consumed and sold for an amount other than the scrap value, or otherwise held in a way that generates economic benefits. If a good or a service is regularly sold separately, then it serves as an indicator that the customer can benefit from a good or service on its own.

As explained in the above section on discounted/free advertising and bonus spots, under Ind AS 115, the transaction price would be allocated to each performance obligation on a relative stand-alone selling price basis.
Carriages fees

Carriage fee means any fee paid by a broadcaster to a Multi System Operator (MSO)/distributor of TV channels, for carriage of the channels of that broadcaster on the distribution platform owned or operated by such a MSO.

A broadcaster also enters into a subscription agreement with a cable company for which cable company agrees to pay the broadcaster a specified amount per subscriber per month during the term of the agreement. A question arises as to whether such revenues should be presented on a gross or net basis by the broadcaster.

There is no explicit guidance under Ind AS 18 on the accounting treatment for the consideration which is payable to a customer; however, Ind AS 115 provides explicit guidance on this topic. As per Ind AS 115, the consideration payable to a customer includes cash amounts that an entity pays or expects to pay to the customer, or to other parties that purchase the entity’s goods or services from the customer. An entity evaluates the consideration payable to a customer to determine whether the amount represents a reduction of the transaction price, a payment for distinct goods or services, or a combination of the two. If the consideration payable to customer does not represent a distinct good or service, then it is accounted for as a reduction of the transaction price.

In the case of carriage fees, the broadcaster receives no identifiable benefit that is sufficiently separable from the sale of its services to the cable operator. This analysis is based on two facts:

1. Any benefit received by broadcaster cannot be separated from the arrangement to sell its services to the cable operator and
2. Commercially the broadcaster could not enter into such an arrangement (for payment of carriage fees) with a party other than the purchaser (cable operators) of its television services, and the fact that the broadcaster has to pay carriage fees would not change even if the cable operator was required to commit to a minimum level of purchases in order to receive the consideration from the broadcaster.

The payments, therefore, should be characterised as a reduction of revenue when recognised in the broadcaster’s statement of profit and loss.

Under Indian GAAP, in the absence of any specific guidance, diverse practices exist and broadcasters account for carriage fees on a gross basis.

Contracts with deferred payment terms

Companies generally enter into syndication deals for selling movies, television episodes, etc. which are long term in nature and may range from two to five years. In case of such contracts, it is possible that payments are over an extended period of time. For example, company A sells three blockbuster movies to company B for INR80 crore and company A agrees to a deferred payment schedule such that the entire sale consideration will be received in 24 equal monthly installments. It is important to note that revenue was recognised by company A on the date of sale, since the tapes were delivered and there was no user restriction period. Under Indian GAAP, the company would have recognised the trade receivable at its nominal amount. Under Ind AS 115, if a contract is deemed to include a significant financing component, then the company will need to adjust the transaction price to reflect the time value of money.

For applying Ind AS 115, companies in India would need to review all the contracts that span a period longer than one year and exercise judgement in assessing whether a significant financing component exists. Additionally, they would need to determine the processes for estimating the discount rates and ensure that the systems can handle the complex calculation that will be needed in certain cases.

Programme assets and similar rights

Various types of ‘rights’ exist in the media and publishing industries. In the media sector, such rights comprise film and television rights held by a television broadcaster or the rights portfolio held by a film producer or rights trader. In the publishing and publicity industry, such rights are primarily publishing, title and distribution rights that a publisher holds for the purposes of exploitation.

Media and publication rights are intangible assets. The key factor is not the physical substance of the book or the film or sound storage medium, but the extensive opportunities to exploit the rights to the content. This gives rise to specific accounting issues.

For example, publishing, title and distribution rights can be generated internally by the publishing company or acquired from third parties. The cost of such rights acquired from third parties should be recognised as an asset because, in many cases, they meet the definition and recognition criteria for an intangible asset, i.e. the entity controls the resource and expects future economic benefits to flow out of it, the cost can be measured reliably, etc. However, the costs associated with internally generated publishing, title, and distribution rights may not be recognised as intangible assets because though they appear to satisfy some of the above criteria, the expenditure on such internally generated rights cannot be distinguished from the cost of developing the publishing company’s business as a whole.

Under Ind AS, programme assets and distribution rights that meet the recognition criteria should be recognised at cost. The cost includes the purchase/production cost and any other directly attributable costs required to exploit the rights.
Amortisation of rights

Content, whether it be a movie, TV serial, music album or advertisement for example, is the premise for a variety of revenue streams in the M&E sector. Given its importance across various verticals in the sector, accounting for content assumes significant importance, including amortisation of cost.

In the Indian context, while Accounting Standard (IAS) 28, Intangible assets and AS 28, Impairment of Assets, lays down the broad principles as there is no specific literature which deals with amortisation of content in the M&E sector and consequently, varied practices have been followed in the industry. For example, in the case of movies, several distribution companies amortise a pre-determined percentage of the film costs in the first year and use other pre-determined rates for future years (the percentages used may vary from one company to another), whereas some companies follow the amortisation principles laid down in the Income Tax Act, 1961. These percentages or methods may or may not reflect the manner in which different individual rights may be exploited.

Under Indian GAAP, the annual amortisation expense for content cost is calculated on the basis of the best estimate of its useful life. Such amortisation should reflect the pattern in which the right is expected to be exploited. The straight-line, units of production, or the unit of production method. The method used for an asset is selected based on the expected pattern of consumption of economic benefits and is consistently applied from period to period, unless there is a change in the expected pattern of consumption of economic benefits to be derived from that asset.

Many of the media companies, including internationally, follow a revenue based amortisation method for film rights (individual film forecast method). The individual film forecast method provides for amortisation of carrying cost of the film rights during a period based on proportion of actual revenues generated during the period to estimated total revenues. It is observed that there is generally higher amortisation in the initial years as they expect to generate revenues primarily in the first few years and believe that the exploitation potential would significantly reduce in subsequent periods. Similarly, in the television segment, a programme asset intended for multiple broadcasts is typically amortised using a diminishing balance of amortisation rates depending on the number of permitted or planned broadcasts. The diminishing balance of the amortisation expense appropriately reflects the decline in value of the programme assets. Experience may show that this value is highest on the first broadcast and falls with subsequent broadcasts or repeats.

Ind AS 38, Intangible Assets and IAS 38, Intangible Assets introduce a rebuttable presumption that the use of revenue-based amortisation methods for intangible assets is inappropriate. This presumption can be overcome only when revenue and consumption of the economic benefits of the intangible asset are ‘highly correlated’, or when the intangible asset is expressed as a measure of revenue.

While this is not an outright prohibition, it creates a hurdle for when revenue-based methods of amortisation may be used for intangible assets. The phrase ‘highly correlated’ is a new term that is not used in other Ind AS(s). It was introduced to limit the use of revenue-based amortisation, because revenue is affected by other inputs and processes, selling activities and changes in sales volumes and prices, which are not directly linked to the consumption of economic benefits embodied in the intangible asset. As a result, a company would need to demonstrate that there is more than just an element of relationship between revenue generation and the consumption of benefits.

Another issue arises if television broadcasters acquire films that may not achieve cash flows in the form of advertising revenue i.e. revenue earned could be less than the cost of the film. The reason why companies may still acquire these expensive films could be to improve their image and increase their market share. This could have a positive knock-on effect on other programmes that are broadcasted before or after the film in question, as well as on the broadcaster’s overall image. These knock-on effects are therefore included in practice, for example, by considering individual advertising spaces (e.g., Saturday evenings) as a cash generating unit when calculating cash flow forecasts, i.e. individual programmes within the advertising space are regarded as interdependent.

IAS 38 is effective 1 January 2016 and Ind AS 38, 1 April 2016. Various companies in the M&E sector appear to be struggling to find an alternative to the revenue based amortisation methodology. While there is no clear methodology which appears to be emerging at this moment, it is one aspect which will need to be thought through carefully so that there is uniformity in application. This will also help ensure comparability of financial statements issued by various players in the industry. Also, as a result, it is likely that many entities may need to change their accounting policy.
Acquisitions and business combinations

With the ongoing consolidation in the media industry, another impact area is accounting for business combinations. These are acquisitions of controlling stakes in entities and businesses like mergers, acquisition of a subsidiary, purchase of net assets of a division, etc. Indian GAAP has varied guidance on accounting for such transactions and allows the pooling of interests method or the purchase method of accounting. Under Ind AS, all business combinations are accounted for at its fair value as on the acquisition date. This process involves the identification of intangibles subsumed within the goodwill like customer relationships, favourable leases, fair valuation of contingent liabilities, contingent consideration and all other acquired assets and liabilities whether recognised or not in the acquiree’s balance sheet. Such a fair value based accounting treatment would ensure appropriate reflection of the factors that affected the negotiation process of the transaction in the financial statements and bring accounting closer to the economic attributes inherent in the business combination. The companies should evaluate the need to align accounting policies, chart of accounts, maintain separate accounting records, etc. after the transaction has been completed. For example, if company A acquires a controlling stake in company B, then post-acquisition, consolidated financial statements of A would be based on the fair value of assets whereas company B’s standalone financial statements would continue at historical cost.

Consolidation

Several companies in this sector operate through multiple legal entities for different businesses. Some of these entities involve the participation of external strategic or financial investors who may hold a significant stake. Under Indian GAAP control is defined as holding more than half of voting power or exercising control over the composition of the Board of Directors.

Under Ind AS, consolidation is based on the concept of ‘control’. Under Ind AS 110, Consolidated Financial Statements, an investor controls an investee when the investor is exposed to, 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. To have power, the investor needs to have existing rights that give it the current ability to direct those relevant activities which significantly affect the investee’s returns. An investor can have power over an investee even if other parties have existing rights to participate in the direction of the relevant activities – e.g. a significant influence over the investee arising from one or more contractual arrangements.

Under Ind AS, power is analysed with the help of voting rights that are substantive, (including substantive potential voting rights), rights arising from other contractual arrangements, de facto power, and through special relationships e.g., structured entities.

The control model in Ind AS 110 is complex and includes numerous indicators to consider; the investor would need to reflect upon all the relevant facts and circumstances in assessing whether it controls an investee and no specific hierarchy for consideration is provided. Thus, while, a majority of voting power would indicate control, it is necessary to evaluate all other facts and circumstances to determine which party has control.

For example, consider an entity where the Indian partner owns 51 percent of the ownership interest and the foreign partner owns the remaining 49 percent. However, certain decisions such as the approval of annual budgets, appointment and remuneration of key management personnel, etc. require an approval of the Board nominees of the foreign partner. Under Ind AS, even though the Indian partner holds 51 per cent, the presence of important veto rights with the minority shareholder may indicate that unilateral control does not vest with the Indian partner. In such a case, the Indian partner would not be able to consolidate this entity as a subsidiary. However, in the above case, if an approval of the Board nominees of the foreign partner is required only for certain decisions like fresh issue of capital, change in the name of the company, acquisition or disposal of business or division, etc. then in such a case, the Indian partner is said to have control over the entity.

Further, there are certain GAAP differences with respect to consolidation procedures as well. Under Ind AS, a company will need to consider its deferred tax impact on unrealised profit arising on intercompany transactions. This may pose additional challenges specifically when one of the companies capitalises the inventory. For example, company B (a subsidiary) has sold its movie library to company A (the parent) and company A has capitalised this movie library and will amortise it over a period of three years. On consolidation, company A would not only have to eliminate the intercompany transaction but also evaluate the deferred tax on such an intercompany transaction.

In addition to the above, there are other differences with respect to accounting for rights licenced, barter transactions and evaluation of whether the company is a principal or an agent, which have been explained in detail in this publication.

To summarise, the M&E sector need to gear up to deal with changes on account of transition to Ind AS. These changes are likely to have an organisation wide impact and are not restricted just to the accounting and finance functions in the company. For example, changes in the IT systems may be required, staff will be needed to be trained for new standards, processes may require some revision, etc. Companies will, therefore, need to plan in advance and invest time to ensure a smooth transition to Ind AS.

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1. Exposure Draft on Ind AS 18, Revenue.
2. Ind AS 115, Revenue from Contracts with Customers.
Conversation with industry leaders

With a view to gain perspective of the industry we have interviewed two CFOs of leading companies from the industry where we explore some of the key accounting, reporting, and topical matters relevant to this industry. We had a conversation with Nitin Nadkarni, Chief Financial Officer, Multi Screen Media Private Limited and Sujit Vaidya, Vice President and Chief Financial Officer, The Walt Disney Company (India) Private Limited.
In conversation with

Nitin Nadkarni  
Chief Financial Officer, Multi Screen Media Private Limited

Sujit Vaidya  
Vice President and Chief Financial Officer, The Walt Disney Company (India) Private Limited

There have been expectations with reference to the growth of the industry based on the FICCI - KPMG Indian Media and Entertainment Industry Report 2015 (FICCI frames report). Eleven months into the calendar year, how do you view the progress of the various sectors of the industry? What are your views on the ‘Digital India’ initiative of the government?

Sujit Vaidya:
Many sectors of the industry have seen growth in the past eleven months. The television sector has seen many regulatory changes over the past 24 months with a positive impact. The investment in the Digital Addressable System (DAS) implementation is underway though its still lagging in some geographies. In terms of subscription, broadcasters are probably still not getting the accurate data and needs to get better. Hence, DAS implementation is patchy at the moment but I believe the direction is right and the industry will get there within the timeframe published. The overall per subscriber revenue has to increase through better packaging, content creation and targeting. Viewers may not pay for non-differentiated content in the crowded offerings. However, sharply defined and targeted offerings/packages will help improving subscription revenue by providing better choice to the consumers as seen by Direct To Home (DTH) operators. However, there is still a long way to go.

Nitin Nadkarni:
The third vertical emerging is the digital and mobile space, which is the best platform to reach the new consumers in affordable manner. Its akin to the ‘sachet’ model which worked very well for the Fast Moving Consumer Goods (FMCG) business. We can create sachets of entertainment and take it to consumers where entertainment is still difficult to reach or unaffordable; e.g. rural areas where screens are restricted or where TV exists but electricity is scarce. Digital media gives the consumer the opportunity to get exposed to high class entertainment which they can consume at reasonable rates and the ‘Digital India’ initiative is a step towards that direction. With the 4G infrastructure developing to ensure better broadband connectivity, it will rival the existing sectors like linear TV. This will create growth avenues for the media and entertainment industry that one has not seen as of today and the content producers have to be geared up for creating specific content for this space.

One area of improvement is that of consistent policy application and execution rigor. Such execution gaps dilute the intended impact of the regulations. For example, with exemptions being made for the advertisement cap in case of news channels, the impact has not fully and equitably taken place as envisaged.

In a nutshell, the policy direction is right, implementation is erratic and the industry participants are responding in a varied manners. However, positive impacts would be seen over the next couple of years rather than instantaneously.

On the Hindi Studio side, the investment in multiplexes screens is still lagging. The number of screens that China has built over the past couple of years versus those in India is significantly higher. We are in a phase where growth in new screens appears to have plateaued and the consolidation in exhibitor business is taking place. There are infrastructural challenges which the government can help overcome to increase the number of screens in India with adequate policy intervention. On the production side, the new movies continue to be made at the same rate as in the past but quality still remains a challenge invariably affecting the box office success. Also, introduction and/or roll-out of government initiatives could also boost the important studio business, e.g. if the entertainment tax is subsumed within Goods and Services Tax (GST), that clarity would help as in some states entertainment tax is as high as 50 percent. Further, according to the status of an industry to the film sector would definitely help the studio business.

As per the FICCI frames report, the television industry was expected to grow at around 14 per cent this year. We have grown at a much higher rate with several channels contributing towards growth. However, the pace of cable digitisation has slackened and addressability has continued to evade the industry. As a result, subscription revenue growth has been relatively modest and carriage fees have risen during the year. Most broadcasters are continuing to enter into bilateral deals with Multi System Operators (MSOs) for subscription revenues as against engaging in per subscriber deals.
The newly introduced ratings system by Broadcast Audience Research Council (BARC) is yet to settle down, especially after extending its coverage to the rural markets. The weightage of rural and Local Circles (LCI) towns is as high as 65 per cent in the sample size, which has skewed the ratings in favour of Free To Air (FTA) channels on DD Direct.

The Telecom Regulatory Authority of India’s (TRAI’s) regulation restricting advertisements to 12 minutes per hour has not directly resulted in an increase in the advertisement rates, which ideally would have been the case in a classic demand-supply market. Though the said ad-cap applies across channels, news channels however enjoy an exemption due to the stay obtained by the News Broadcasters Association. Also, TRAI’s 12 minute ad-cap is not being strictly adhered to by all – there would be instances where some channels extend their ad time to say 13 or 14 minutes. Whilst this issue does not appear to be a priority for the government and TRAI has not taken a tough stand on the violations, broadcasters are self-complying to be in line with the regulation. Incidentally, for sports channels, the 12 minute ad-cap is difficult to follow as advertising can happen only during natural breaks in the play - for example, in a football match, advertising can happen only before and after the match and during half time.

The growth of digital media such as 4G, Internet Protocol Television (IPTV) and broadband TV in India is an opportunity; even though in the long run it poses a threat in terms of diversion of audiences from television to the digital medium. The transition may however take some time given the development stage of infrastructure and the fact that the rollout of 4G services is still in its initial stage.

Our organisation believes that digital is a huge growth area and has developed Sony LIV as our platform. The advent of 4G services, continuing growth in 3G subscribers and the expected growth in internet penetration under the “Digital India” initiative will result in huge growth for digital businesses.

The Companies Act 2013, (the 2013 Act) has introduced various changes. What has been your overall evaluation of the 2013 Act and how have you approached its implementation?

Nitin Nadkarni:
There is no doubt that a revamp of the Companies Act, 1956 was required. However, the ease of implementation in the 2013 Act is missing. A lot of confusion has been created as a result of various notifications and amendments surfacing subsequently as well as due to the lack of clarity on various issues. This suggests that 2013 Act was not thought through thoroughly and may be some aspects could have been pre-empted and fully baked into the 2013 Act. Even now, there are many provisions relating to amalgamations and mergers, winding-up, etc. that have not been notified. The schedule related to the activities covered under Corporate Social Responsibility (CSR) has been amended at least three times since its notification. In my opinion, what could have been done differently was to have a much better planned rollout rather than hastily putting up something. Also, if the industry representations were given enough consideration while drafting the regulations, it would have reduced confusion and helped enhance the implementation ease.

Sujit Vaidya:

We started quite early on Ind AS, as soon as the initial discussion papers were out. We engaged with our statutory auditors so that we interpret it together as it evolved. This kind of an approach avoids disagreements or different interpretations at the time of closure of accounts. There are quite a few areas which required engagement with the business folks as changes in Ind AS impact the way we do business as well as negotiate with key vendors. We engaged with various business leaders to make them aware of the changes. This has shown us the results and we are now aware of the impacts on key areas. Hopefully, there will not be a difference in approach between corporates, regulators, statutory auditors and tax advisors. On the ERP side, we had to make some changes; however, those were not significant.

The Income Computation and Disclosure Standards (ICDS) have been notified and are applicable from Assessment Year 2016-17 onwards. The adoption of ICDS is expected to significantly alter the way companies compute their taxable income, as many of the concepts from the existing Indian GAAP have been modified. This may also require changes to existing processes and systems. What are the key implementation challenges of ICDS that you foresee?

Sujit Vaidya:

The way we approached ICDS was to relook at the existing corporate structure and tax positions, and identify what needs to be changed or managed. There are many changes to be made over the next couple of years as it involves engagement with other regulators like Ministry of Information and Broadcasting (MIB), which can be challenging. This may have a deep impact on the current corporate and tax structures followed by the M&E industry.

1. Enterprise Resource Planning
The three big changes namely the Ind AS, ICDS and the 2013 Act, in my opinion are steps in the right direction and are pegged on the right premises to improve governance in the long-term. However, the government could engage better in terms of the communication and timing with the various stakeholders be it regulators, corporate or professional bodies.

The GST is a path breaking business reform, and not just a tax reform for India. It is likely that GST will be introduced during the Financial Year 2016-17. The GST Bill in its current form, allows local bodies such as panchayats and municipalities to levy and collect the tax. The film industry was hoping that entertainment tax collected by local bodies would be subsumed under GST, but as per the GST bill, this tax would be above the state and central GST on entertainment. Consequent to that, The Film & Television Producers Guild of India has urged the government to fully subsume local bodies’ entertainment tax under the proposed GST. The local body entry tax such as octroi is estimated at INR14,000 crore a year for Maharashtra alone and it has been fully subsumed in the proposed GST. However, the local body entertainment tax that has been estimated at INR25-30 crore across India, has been kept out.

Viewed from this perspective, how are you approaching this area and framing your plans in order to achieve significant efficiencies in business and yielding a competitive edge in the market?

Nitin Nadkarni:
I agree that GST is a path breaking business reform and not just one related to tax. India needs to implement GST at the earliest. However, a lot of ambiguity still surrounds the current GST draft with respect to the broadcasting industry. From the perspective of this industry, a clarity is required on issues such as
(a) Place of supply rules for advertisement sales and broadcasting services
(b) Cross-utilisation of credits between central GST/state GST and state GST credit of one state being allowed to be set off against state GST liability in another state
(c) Compliance and assessment proceedings.

Finally, entertainment tax needs to be subsumed in its entirety under GST; or at the least, the GST Bill needs to impose restrictions (in terms of the number of years or the tax rates) on the powers of the local bodies to impose these taxes. At this point in time, I would say I am a little apprehensive considering the track record of implementation of new regulations, as these generally pose difficulty in the short-term. Internally, GST would demand a lot of changes to our structure and IT systems.

The 2013 Act has introduced Internal Financial Controls (IFC) to be followed by the company and requires that such internal controls are adequate and operating effectively. How have you approached this area and what have been the essential considerations relating to the implementation of reporting on an IFC?

Nitin Nadkarni:
One area where I feel more comfortable is IFC, given that we are already under the full scope of SOX. Major areas like revenue, amortisation, control documentation, etc. are covered by SOX. Nonetheless, there are still some areas such as payroll and fixed assets which are not covered under SOX and are currently being worked on. If implemented correctly, an IFC could go a long way in improving the way the industry functions and help bring about better governance in conjunction with the Companies Act.

Lastly, do you have any regulatory wishlist? Any thoughts on how things could be done better in the sector?

Sujit Vaidya:
I would suggest a forum for the M&E industry, as its practices are quite unique and industry players need to understand what Ind AS and ICDS means for these businesses. It would really help if professionals from various sub-sectors of the media got together and engage in a more productive manner with policymakers and regulators, such that execution challenges, be it on the infrastructure side, how the transactions on the IP and other content are structured, piracy issues which serve as a leakage point for revenue, affiliate sales, etc. are suitably addressed. The size and scale of this industry has grown and has a potential for tremendous employment generation, which I believe is not fully understood and appreciated by the policymakers. We need to get together as an industry and impress the policymakers even further.

Nitin Nadkarni:
While the ease of doing business in India is on the government’s agenda, the ground reality is different and that needs to change. For example, we have channels waiting to be launched for a long time now but the delay caused in the issue of licences by the Ministry is becoming a roadblock. Another example is the issues on service tax, wherein there have been bizarre interpretations of law taken by the department, resulting in huge tax claims and unnecessary litigation. A clarity and stability in the regulations and facilitation of easier execution is something that the industry wishes for.
Barter arrangements

This article aims to:
- Highlight the accounting principles for M&E sector in the case of barter arrangements.

The Indian M&E sector is growing at a rapid pace with the audience transitioning from the traditional mediums of film, television, print and radio to newer means of communication such as digital, social media, etc. The development of newer mediums has resulted in companies in the industry entering into many complex arrangements, with the traditional guidance and standards subject to complex judgements and interpretations; one such area being accounting for barter arrangements.

The definition of revenue under Accounting Standard (AS) 9, Revenue Recognition has following elements as depicted in the diagram below:

A barter arrangement is a scenario wherein two parties enter into a transaction to exchange similar or dissimilar goods or services i.e. there is no circulation of money in the transaction. Although AS 9 does not provide any specific guidance on accounting for such arrangements, the Guidance Note on Dot-Com companies (guidance note) issued by the Institute of Chartered Accountants of India provides some insights into accounting for barter arrangements (such accounting is line with the International Financial Reporting Standards (IFRS)).

Barter arrangements should be recorded based on the fair values of assets (or services) involved. The fair value of the asset surrendered or services provided to acquire the asset or obtain the service should be recognised as cost. The fair value of the asset or service received should be used to measure the cost if this is more clearly evident. Revenue from barter arrangements should be recognised subject to meeting the other principles of revenue recognition like presence of a consideration, transfer of significant risks and rewards of ownership to the buyer and reasonable certainty regarding amount of consideration to be received against such sale of goods.
A company recognises revenue from transactions involving exchange of goods or services, only if the transactions have commercial substance. This is assessed by considering the extent to which future cash flows are expected to change as a result of the transaction. More specifically, an exchange transaction has commercial substance, if the configuration of cash flows (i.e. the risk, timing and uncertainty) of the assets received and transferred are different. Generally, no revenue from barter transactions involving exchange of similar goods or services is recognised.

Advertising companies may enter into arrangements for reciprocal advertisements on each other’s media without cash consideration. There will be a need to use judgement while determining whether the exchange of advertisement services is similar in nature and hence, no revenue might need to be recognised. Based on an analysis of the guidance note, the revenue from advertising barter transactions should be recognised only when the fair values of ‘similar comparable transactions’ are readily determinable from the entity’s history. For determining the fair value, in identifying the advertising space surrendered for cash which is to be considered ‘similar’ to the advertising space being surrendered in the barter transaction, the following factors given in the diagram below need to be considered:

### Comparable
- The transaction should have taken place with an unrelated buyer not later than six months preceding the sale of similar advertising transactions.
- If the economic circumstances have changed, then a shorter, more representative period should be used.

### Similar
- Circulation, exposure or saturation within an intended market
- Timing (time of day, day of week, daily/weekly, 24 hours a day/seven days a week and season of the year)
- Prominence (page on the website, section of periodical, location on the page and size of the advertisement)
- Demographics of readers, viewers, or customers
- Duration (length of time for which the advertisement will be displayed)

Source: Guidance Note on Dot-Com companies

If the above indicators indicate that dissimilar services have been exchanged and the amount of revenue can be reliably measured in a similar comparable transaction, revenues are recognised at the time when the services are provided and equivalent costs are recognised when the corresponding services are utilised. By contrast, the exchange of similar services or services whose fair value cannot be reliably measured, does not result in any revenue/cost recognition.

Some companies believe that barter arrangements are tax neutral because there is no exchange of money. However, this is debatable and the fair market value of goods and services exchanged might be required to be added to the income and cost of both the parties to the exchange and the tax consideration (withholding tax, service tax and value added tax) needs to be analysed under the relevant provisions of the respective laws.
Ind AS 115, Revenue from Contracts with Customers, does not contain specific guidance on the accounting for barter transactions, involving advertising services. Therefore, the general principles of measuring non-cash considerations apply. A non-cash consideration received from a customer is measured at its fair value. If an entity cannot make a reasonable estimate of the fair value, an entity refers to the estimated selling price of the promised goods or services.

Ind AS 115 also scopes out non-monetary exchanges between entities in the same line of business that facilitate sales to customers other than parties to the exchange. Accordingly, revenue from such a barter transaction is required to be recognised by the service provider, if dissimilar services are exchanged. As stated above, the dissimilarity in services is required to be analysed by considering factors such as the nature of the media (television, print, radio, etc.), target audience, frequency, timing, etc.

Example 1: ABC is a broadcasting channel and produces many reality shows. One of its flagship shows, ‘Last Man Standing’ is a high budget reality game show broadcasted on weekends and requires high production value. Hence, ABC has entered into an arrangement with two companies i.e. PQR News and D.com for being the title sponsors for its show. One of the companies, PQR News is a newspaper with pan India presence. ABC and PQR News enter into a sponsorship agreement and the terms of the arrangement are as follows:

- PQR News would be the co-sponsor for the show and consequently, its logos would be presented during the entire tenure of the show i.e. 10 weeks.
- PQR News shall advertise the reality show on all weekdays i.e. Monday – Thursday give a full page advertisement on the first page of its newspaper and the first and last page on the weekends i.e. Friday to Sunday.

ABC charged INR 100 lakh from D.com towards co-sponsorship of the show. PQR News generally charges INR 1 lakh per day for a full page advertisement.

We need to determine whether both the parties ABC and PQR News need to account for this transaction and need to determine the amount of revenue and cost to be recognised.

The provisions of AS 9 read with the guidance note lays down the basic principles for accounting of such transactions i.e. revenue from dissimilar services. Revenue includes the gross inflow of cash, receivables and other consideration received or receivable for goods sold or service rendered. Thus, the term ‘other consideration’ would include a non-monetary i.e. barter arrangement and hence both, ABC and PQR News need to account for revenue and their corresponding costs.

The fair value of the asset surrendered to obtain the service should be recognised as a cost for the service acquired. The fair value of the assets received should be recognised as revenue.

ABC will recognise the value of the asset surrendered as cost. In this arrangement, there is a co-sponsor who has paid INR 100 lakh, thus value of assets surrendered in a similar and comparable transaction is INR 100 lakh which would be recognised as cost in the books of ABC.

In exchange for sponsorship, ABC has received advertisement space in PQR News, the value of which is INR 100 lakh (four weekdays – INR 1 lakh per day for four days and three weekend – INR 2 lakh per day for three days i.e. INR 10 lakh per week). ABC should account for the revenue of INR 100 lakh (as the show will run for 10 weeks).

As far as PQR News is concerned, a question often arises as to whether the cost to be recognised by PQR News is INR 100 lakh or nil (i.e. INR 100 lakh cost net of revenue of INR 100 lakh)

The revenue receivable and cost incurred is towards the exchange of a dissimilar set of services/products; accordingly, revenue and cost need to be accounted for at gross amounts and not netted off. Further, the timing for recognition of revenue and cost would differ as revenue would accrue to PQR News on a daily basis while cost would be incurred proportionately during the duration of the show (10 weeks). Though revenue and cost over the term of the contract would be the same but due to the timing difference, the amount of revenue and cost in a financial year may differ.

Example 2: In continuation of example 1, if PQR News was the only sponsor for the show

Last year, during the previous season of the same show, there were two sponsors who paid INR 75 lakh each. In the current season of the show is replacing another flagship show of the channel, ‘Singing Talent’ for which its title sponsor paid INR 200 lakh.

PQR News being the only sponsor for the show, ABC would determine the cost based on the fair value of the asset surrendered in a ‘comparable similar transaction’. Even though the deal value for the previous season of the show is similar, however it is not comparable as it does not factor changes in the economic factors prevailing in the market today as compared to the previous year.

The deal value for the show ‘Singing Talent’ can be considered to be the appropriate fair value in the above transaction, as it is recent and takes into consideration all the current economic conditions prevailing in the market. Further, it is similar in terms of factors such as exposure within an intended market, timing (same time and three days a week), prominence, demographics of viewers but, the duration of both the shows differ. As most of the factors of the two shows are similar, it could be concluded as a comparable similar transaction and ABC would account for INR 200 lakh towards cost.
Example 3: The Ministry for Information and Broadcasting (MIB) has issued a notice to the channel in respect of the format and content of the show on account of which it has temporarily been discontinued. The show would resume once a clearance has been obtained from the MIB. PQR News is planning not to print the daily advertisement for the show as it may impact its brand image. The arrangement at this stage does not meet the principles of revenue recognition in terms of the future economic benefit following to the parties and its certainty. Thus, revenue and cost should not be recognised during this period (prior to obtaining regulatory approval) by both the parties.

Some other examples of barter transactions in the M&E sector are as below:

- In the case of a movie, the arrangement may be as follows: The producer provides an in-film advertisement to a customer, who in turn advertises the movie on his medium e.g. a producer displays a particular TV channel in the film and in return, the TV channel allocates promotion time for the film on its channel or, the customer finances the cost of the vehicles or provides them free of cost and in return the film advertises its vehicles (products) using stills from the film.

- An event management company in lieu of advertisement space at the event, receives products/services from such companies, which is then sold at the event at a premium value.

Conclusion:

Though many companies as a practice, currently do not account for barter transactions in India, the appropriate accounting for barter transactions is essential to accurately represent the revenue and cost of companies as also to discharge their statutory tax obligations.
Gross versus net accounting

This article aims to:
- Highlight the challenges faced by M&E sector in accounting for revenue transactions.
- Provide various revenue models adopted by the sector.

The Indian M&E sector has witnessed significant changes in terms of use of technology, newer markets and means of exploitation. Although these developments present exciting new opportunities, they also pose new challenges on the accounting front, including those of revenue transactions. One such aspect is whether revenue should be reported at gross or net amounts.

Principal – agent relationship
AS 9, Revenue Recognition defines revenue as the gross inflow of cash, receivables or other consideration arising in the course of the ordinary activities of an enterprise from the sale of goods, rendering of services, and from the use by others of enterprise resources yielding interest, royalties and dividends. Revenue is measured by the charges made to customers or clients for goods supplied and services rendered to them and by the charges and rewards arising from the use of resources by them. In an agency relationship, revenue is the amount of commission and not the gross inflow of cash, receivables or other consideration.

As per the above definition, revenue represents the amount receivable by an entity for its own account. Therefore, for a principal, revenue should be presented at its gross amount and is measured before deducting related costs. In an agency relationship, the amounts collected on behalf of and passed on to the principal is not revenue of the agent. The revenue of the agent is the amount of commission, plus any other amount charged by the agent to the principal or other parties. However, the standard does not specifically detail the factors to be considered in determining a principal – agent relationship. This determination is therefore based on an evaluation of the risks and responsibilities undertaken by the entity. Some of the factors which are generally evaluated globally include:

- The customer’s understanding of the primary obligor in the arrangement
- The entity’s ability to set the selling price with the customer
- Which entity assumes inventory risk
- Which entity assumes credit risk
- Whether the entity performs part of the services provided or modifies the goods supplied.

The above factors are not necessarily conclusive but only indicative. An entity that undertakes responsibility for majority of the factors listed above is usually the party which accounts for revenue on a gross basis. The evaluation could still differ based on specific terms of the agreement between the parties and entities would need to exercise significant judgement.
In the case of a typical distributor-exhibitor revenue sharing arrangement, an exhibitor is the primary obligor to the patrons for exhibiting the film and also to the government towards deposit of entertainment tax. The business is largely a cash trade and thus the exhibitor generally is not exposed to any significant credit risk except probably in the case of corporate bookings. Further, the charges for the services being ticket prices, are decided by the exhibitor. While the exhibitor does not have any inventory risk in terms of the recoverability of the cost of the film, the risk in terms of the occupancy levels at the theatre are with the exhibitor and has a direct bearing on the exhibitor’s ability to recover fixed costs. Therefore, in such a scenario, the exhibitor records the gross proceeds from the sale of tickets, net of entertainment tax and discounts, as revenue.

**Producer - distributor**

A producer-distributor relationship, could have following models:

- **Outright sale** (all rights in the movie are sold to a distributor for a lump sum consideration)
- **Minimum guarantee plus revenue sharing** (the distributor is to pay an upfront lump sum fees and a revenue collection beyond minimum guaranteed/lump sum amount shall be shared between the parties)
- **A pure revenue share** (collections to be distributed at an agreed percentage).

The transaction between parties would be on a principal to principal basis if the distributor,

- is the primary obligor in his dealings with exhibitors
- assumes credit risk towards the collection of revenue share from the exhibitor
- has the inventory risk in case of outright sale or minimum guarantee arrangements and is responsible for delivery of the film to the exhibitor.

The distributor would record revenue received from the exhibitor, net of the latter’s share, on a gross basis and the producer’s share as his cost. Consequently, the producer would record only his share of revenue from the distributor.
Advertising slots – customer and advertising agency relationship

Advertising agencies provide services to customers intending to promote their products/services through various media such as television channels, print, radio and the digital platform. At the behest of such customers, agencies arrange for advertising slots and either charge commission at a fixed rate or markup the slot price for their fees, generally 12 to 20 per cent of the price charged by media owners.

The customer and the agency enter into arrangements for purchase of advertising slots. The various indicators to determine whether the advertising agency should recognise revenue on a gross or net basis may be evaluated as under:

- The media owner is the primary obligor in the transaction. The display of an advertisement provided by the customer is the sole responsibility of the media owner and it is entitled to compensate or waive charges for any deficiency in this regard. In case of a dispute, the advertising agency may only act as a mediator.
- While the advertising agency helps negotiate the slot rates, these are primarily determined by the media owner. The media owner could charge different rates to different customers at its sole discretion.
- The advertising agency does not usually have any inventory risk as it is not responsible for any unsold inventory of the media owner. There could be arrangements though, where certain media inventory is committed to be taken by the agency and hence, would require careful evaluation based on facts and circumstances of each case.
- The advertising agency assumes the credit risk for collection from the customers. Except for disputed cases, the advertising agency is required to pay for the media consumed even if the customer defaults or fails to honour the arrangement e.g. it cancels the advertisement at the last moment.
- The customer pays the advertising agency, slot rate plus marked up fees and the agency in turn pays the slot rates to the media owner. Service tax, wherever applicable, is levied on the gross amounts billed by the respective parties.

Based on the above facts and indicators, it seems that majority of them support the fact that an advertising agency is acting as an agent in the transaction; though some indicators such as credit risk, may support gross accounting and further evaluation would be required. Generally an advertising agency would recognise revenue on a net basis i.e. only its share of revenue.

Advertising agency would act as a principal in cases where the advertising agency purchases fixed advertising slots or commits to media owner on its own accord without being specifically engaged by a customer. There could also be a scenario wherein an advertising agency enters into a multiple element contract with its customers and accounting could vary for the different elements.

Let us consider the following example:

ABC Limited (an online shopping business) has approached XYZ Limited (an advertising agency) to create an advertisement for their ‘INR Million Sale Day’ and to place the same in a leading newspaper on the front page. The payment terms as per a signed estimate between ABC Limited and XYZ Limited is INR5 lakh for creative work and fixed agency commission for placing the advertisement in the newspaper.

XYZ Limited has approached B News (a leading newspaper) to place their client’s advertisement for a fixed consideration of INR15 lakh. XYZ Limited will raise separate invoices for the creative work as well as the media business; with creative work taking INR5 lakh and advertisement space for INR16 lakh.

XYZ Limited would have to evaluate whether it is acting as an agent or principal for the two services: creative services and placement of advertisement in the newspaper. XYZ Limited will evaluate all facts and circumstances and apply its judgement while evaluating the various factors to check if it is acting as a principal or an agent.

If after the evaluation of the various factors it seems that XYZ Limited is acting as a principal for providing creative services then it would recognise revenue of INR5 lakh. While for advertisement space, if XYZ Limited is acting as an agent then it would recognise commission (INR1 lakh) as its revenue (net amount).
Television broadcasting – accounting for revenue from reality shows

In recent times, a lot of television channels broadcast reality and game shows where the viewers are required to vote in order to participate in the show. The voting takes place through SMS, call or online participation. Telecom companies charge special rates for these calls/SMSs and television broadcasters enter into revenue sharing arrangements with the telecom companies for such voting. The question therefore arises whether the television channel should recognise revenue from voting on a gross or net basis.

Let us consider the following example: PQR Network, a television channel, has produced a weekly show named Singing Stars, where new aspiring singers participate and the television viewers are required to vote for their favourite contestant in order for them to succeed and win the show. A viewer votes for a contestant through SMS and gets charged INR15 in his monthly mobile bill by Mobile Today (a telecom company). The arrangement between the parties is that Mobile Today will share 40 per cent of the revenue from such service with PQR Network. The question is whether PQR Network is required to account for revenue on a gross or net basis.

**Scenario 1: Gross accounting (principal-to-principal basis)**

PQR Network accounts INR15 as revenue and INR9 as cost towards revenue share of Mobile Today.

**Scenario 2: Net accounting (principal to agent basis)**

PQR Network accounts INR6 as revenue.

The indicators that Mobile Today should account for revenue on gross basis are as follows:

- Mobile Today is responsible for providing services to the customer i.e. call, SMS and data for which it incurs expenses towards building the network infrastructure.
- Assumes credit risk in case any of its postpaid customer defaults in payment of bills.
- Responsible for payment of taxes
- Rates for call, SMS and internet data are decided by the telecom company
- Responsible for compliances with the Telecom Regulatory Authority of India (TRAI) regulations.

Based on above analysis, in the normal course of business, the television broadcaster would account for revenue from such services on a net basis.

**Conclusion**

Recording of revenue on a gross or net basis requires careful consideration and should be evaluated on a case to case basis after considering all facts and circumstances.
Revenue from sale of rights

In the M&E sector, the owner of the content monetises the rights therein either on their own or through a grant of rights to third parties for further exploitation. Such grant of rights may either be in perpetuity or for a specific period of time. Moreover, it is quite common for the owner to grant the rights prior to the content being ready or otherwise available for exploitation. For example, producers of movies often sell rights such as those related to music, satellite, merchandising, etc. before the actual release of the movie. Also, in some cases, these agreements contain a restriction period within which the rights cannot be exploited by the acquirer or a condition such that the rights are available for exploitation to the acquirer only after a specified date. For example, satellite rights may be sold with a condition that the movie can be telecast by the broadcaster only after the expiry of two months from the first theatrical release of the movie. In such cases, the issue arises as to what should be the appropriate time of revenue recognition for the content owner(s).

Paragraph 4 of Accounting Standard (AS) 9, *Revenue Recognition* defines revenue as the gross inflow of cash, receivables or other consideration arising in the course of the ordinary activities of an enterprise from the sale of goods, rendering of services, and from the use by others of enterprise resources yielding interest, royalties and dividends. Revenue is measured by the charges quoted to customers or clients for goods supplied and services rendered and by the charges and rewards arising from the use of resources by them.

As per paragraph 10 of AS 9, revenue from sales or service transactions should be recognised, provided that at the time of performance it is not unreasonable to expect ultimate collection. If at the time of raising of any claim it is unreasonable to expect ultimate collection, then revenue recognition should be postponed.

As per paragraph 11 of AS 9, revenue from the sale of goods shall be recognised when all the following conditions have been satisfied:

a. The seller of goods has transferred to the buyer the property in the goods for a price, or all significant risks and rewards of ownership have been transferred to the buyer and the seller retains no effective control of the goods transferred to a degree usually associated with ownership;

b. No significant uncertainty exists regarding the amount of the consideration that will be derived from the sale of goods.
Though many of the general principles of revenue recognition are met with at the time of delivery of content, the fact that the licensor retains effective control by way of precluding the licensee to exploit the right, is enough reason to defer revenue recognition till the time rights become active as it can be argued that the entity has not parted with effective control of the rights.

The above principles will apply even under exposure drafts of Ind AS 18, Revenue, and Ind AS 115, Revenue from Contracts with Customers.

In practice, many companies in India do not defer revenue recognition even if there is a restriction on the broadcaster/Direct To Home (DTH) operator to telecast prior to a specific date. This is based on the argument that once the tapes are delivered to the broadcaster and payment has been received, all the criteria for revenue recognition are met with and the restriction on telecast till a particular date probably is only protective in nature. Furthermore, the broadcaster is usually able to deal with the rights as desired e.g. the broadcaster may sub-lease the rights for its contract period and monetise it prior to the commencement of the telecast period. However, since the broadcaster’s ability to use commences only on the telecast commencement date, the control and the attached risks are deemed to pass only after the effective date. Even in case of a further sub-lease, though money is realised by the broadcaster, it is for the contract period commencing on the first telecast date. In our view, revenue recognition should therefore be postponed till such a date.

Some other similar scenarios related to the timing of revenue recognition are as follows:

- Sale of music or home video rights: Revenue from the sale of music or home video rights would be recognised at the time of agreement even though the agreement is executed prior to the release of the movie, if there is no restriction to exploit the music rights or market the DVDs, blue ray discs, etc. to the public.

- Sale of merchandising rights: Revenue from the sale of merchandising rights would be recognised when
  1. Risks and rewards of ownership of the merchandise have been transferred to the buyer and the seller retains no effective control of the goods transferred to a degree usually associated with ownership;
  2. No significant uncertainty exists regarding the amount of the consideration that will be derived from the sale of goods.
Tax issues pertaining to the M&E sector

While the M&E sector is witnessing a robust business growth and transformation, the tax issues surrounding the industry have also kept pace with the growth. It would not be incorrect to state that it is the need of the hour to resolve some of the long outstanding tax issues faced by the industry and provide an impetus for further growth.

The current government came into power last year with a promise of a non-adversarial tax regime and echoed its strong intention to effectuate changes for the ease of doing business in India. With this definite intent, the Finance Minister unveiled his first full budget in February this year, which not only fortified his clear commitment of putting before the country and the global diaspora a non-adversarial and a stable tax regime, but also strengthened the positive outlook with which India is now viewed globally. His proposals to defer the General Anti-Avoidance Rules (GAAR), reduce tax on royalties and Fees for Technical Services (FTS) payable to non-residents, implement the Goods and Services Tax (GST) regime from 1 April 2016, have helped to lay down an optimistic road map for the industry.

Having said that, the M&E sector continues to struggle with several other issues such as withholding tax on various payments made by the broadcasters, withholding tax on discount on sale of set top boxes/recharge coupon vouchers in the case of Direct To Home (DTH) industry, uncertainty surrounding the taxation of a digital economy, foreign sports associations, teams and players, dual levy of indirect taxes on various activities, loss of input CENVAT credit and the likewise.

This article aims to:
- Furnish the distinct attributes of the M&E sector and highlight key tax issues impacting it.
The Income-tax Rules, 1962 (Rule 9A and 9B) permit the deduction of expenditure incurred on production of films/acquisition of distribution rights therein either in the first year of release or over a period of two years, based on when the copyrights/distribution rights in the films are exploited or depending on the date of release of the film.

There are several ambiguities surrounding the applicability of Rule 9A/9B. These relate to whether the rules extend to satellite, music, home video and other rights in addition to theatrical rights, whether it is directory or mandatory in nature, whether it overrides all other provisions of the Income-tax Act, 1961 (IT Act), deductibility of expenses which are not covered under these Rules, etc.

Another issue which the film industry is currently struggling with is the levying of withholding tax at the rate of 10 per cent (under Section 194J of the IT Act) on an amount received towards the grant of a copyright in content (for example, satellite rights, home video rights, music rights, etc.). The industry considers this withholding rate as excessive, considering the profit margins prevalent in the industry and the potential adverse impact on the taxpayers’ cash flows.

Simultaneously, the industry is also grappling with issues on the indirect tax front as well. Licensing of non-theatrical rights is subject to service tax and at the same time the state VAT Acts have included copyrights in the list of intangible goods bringing it within the purview of VAT applicability. Thus, licensing of a copyright is subject to a dual levy of VAT as well as service tax, a serious concern which needs to be addressed by the state as well as central government in consensus with each other.

Under the proposed GST regime as well, it will be of prime importance that the activity of licensing of a copyright is clearly defined as a supply of service or goods. If the same is not appropriately classified under the law, then it is likely that the dispute as to whether the said activity is a supply of service or goods will continue, as there is a possibility that the rates for services and goods can differ under the GST scenario.

In addition to the above, the benefit of an exemption granted to licensing of theatrical rights has also not been very useful to the industry. Though the said activity is under the list of services exempt from the levy of service tax, a large portion of input services availed by the producer/copyright owner (such as services provided by actors and technicians) is liable to service tax from 1 July 2012. Thus, there is significant loss of CENVAT credit on the said input services attributable to revenue earned from licensing of theatrical rights. This is a huge cost for film producers/copyright owners.

Some of the key tax issues impacting the M&E sector are discussed below:

Film industry

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There are several ambiguities surrounding the applicability of Rule 9A/9B. These relate to whether the rules extend to satellite, music, home video and other rights in addition to theatrical rights, whether it is directory or mandatory in nature, whether it overrides all other provisions of the Income-tax Act, 1961 (IT Act), deductibility of expenses which are not covered under these Rules, etc.

Another issue which the film industry is currently struggling with is the levying of withholding tax at the rate of 10 per cent (under Section 194J of the IT Act) on an amount received towards the grant of a copyright in content (for example, satellite rights, home video rights, music rights, etc.). The industry considers this withholding rate as excessive, considering the profit margins prevalent in the industry and the potential adverse impact on the taxpayers’ cash flows.

Simultaneously, the industry is also grappling with issues on the indirect tax front as well. Licensing of non-theatrical rights is subject to service tax and at the same time the state VAT Acts have included copyrights in the list of intangible goods bringing it within the purview of VAT applicability. Thus, licensing of a copyright is subject to a dual levy of VAT as well as service tax, a serious concern which needs to be addressed by the state as well as central government in consensus with each other.

Under the proposed GST regime as well, it will be of prime importance that the activity of licensing of a copyright is clearly defined as a supply of service or goods. If the same is not appropriately classified under the law, then it is likely that the dispute as to whether the said activity is a supply of service or goods will continue, as there is a possibility that the rates for services and goods can differ under the GST scenario.

In addition to the above, the benefit of an exemption granted to licensing of theatrical rights has also not been very useful to the industry. Though the said activity is under the list of services exempt from the levy of service tax, a large portion of input services availed by the producer/copyright owner (such as services provided by actors and technicians) is liable to service tax from 1 July 2012. Thus, there is significant loss of CENVAT credit on the said input services attributable to revenue earned from licensing of theatrical rights. This is a huge cost for film producers/copyright owners.
Advertising agencies purchase advertisement airtime at a customary discount of 15 per cent from the broadcasters for placement of advertisements of their clients on the television channels.

The tax authorities have been contending that such a discount is in the nature of commission/brokerage paid by television channels to advertising agencies and accordingly, liable to withholding tax at 10 per cent under Section 194H of the IT Act.

However, taxpayers believe that the aforesaid discount given to advertising agencies is not in the nature of ‘commission or brokerage’ and hence are not liable to Tax Deduction at Source (TDS) under Section 194H of the IT Act. The above controversy has resulted in protracted litigation and thus a clarification on the matter is awaited from the government.

Further, broadcasting companies make significant payments to software production houses towards production of TV programmes. They also pay placement/carriage fees to DTH operators, multi system operators and various cable operators towards placement/carriage of the channels. The channel companies have been contending that such payments attract TDS under Section 194C of the IT Act at a rate of 2 per cent. However, the tax authorities on the other hand are of the view that such payments are liable for TDS at 10 per cent on the ground that the payments are towards FTS/royalty. This has again resulted in protracted litigation.

Another issue adversely impacting broadcasting companies is the treatment of payments of transponder hire charges made by them to the satellite companies for transmission of their TV signals as royalty under the retrospectively amended IT Act.

In this regard, it is worthwhile to note that non-resident taxpayers can continue to take the benefit of tax treaties entered into with India to contend that such a payment is not in the nature of ‘royalty’ under the tax treaty and hence, not liable to tax in India. However, one needs to be mindful of the decision of the Mumbai Tribunal in the case of Viacom 18 Media (P) Ltd1. wherein it was held that post the retrospective amendment in the IT Act, payments for transponder hire charges are taxable as ‘royalty’ even under the tax treaty.

Taxation of foreign telecasting companies in India has also been a vexed issue. Generally, these companies are taxable in India provided they have a business connection/Permanent Establishment (PE) in India. Taxation in such cases is only on the income which is attributable to the PE/operations carried out in India. The circumstances under which the Foreign Telecasting Companies (FTCs) constitute a PE/business connection in India and the determination of income attributable to such PE/operations carried out in India, continues to be a contentious issue between the FTCs and tax authorities.

DTH industry

An issue that has been bothering the DTH industry is whether it is required to withhold tax on the amount of discount given to distributors on the sale of Set Top Boxes (STBs)/Recharge Coupon Vouchers (RCVs). The tax authorities are of the view that discount on sale of STBs/RCVs is in the nature of commission. Therefore such discount is subject to withholding tax at the rate of 10 per cent under Section 194H of the IT Act. However, the industry is of the view that the discount is not in the nature of commission and hence, Section 194H is not attracted thereon.

The DTH industry is facing multiple issues on an indirect tax front as well. The industry is burdened with multiplicity of taxes on various transactions/activities such as service tax and entertainment tax on subscription charges, licence fees payable to the government on revenue earned, etc.

Currently the industry is dealing with issues on a dual levy of VAT and service tax on certain activities. Many of the DTH players do not sell STBs and treat them as goods used in provision of services or provide the STBs to the subscribers on an entrustment basis without consideration. There is no supply/sale of STBs that takes place from the DTH player to the subscribers. However, VAT authorities of various states are seeking to levy VAT on such an activity on the ground that the activation/installation charges recovered from customers are towards the price of STBs.

Also, taxation of RCVs has been a subject matter of dispute for quite some time as to whether the same should qualify as goods and be subject to VAT or should be treated as a service and be liable to service tax.

While there are judicial pronouncements which held that RCVs do not qualify as goods, it would be beneficial if the state VAT authorities issue clarifications under their respective VAT Acts to resolve all the ambiguity floating with regards to classification of RCVs as good or services.

Thus, just as the classification of an activity of licensing of copyrights is of importance under the GST regime, similarly, a classification of STBs/RCVs is also relevant under the proposed new law to reduce the chances of probable litigation.

1. Viacom 18 Media (P) Ltd. vs ADIT [2014] 66 SOT 18 (Mum Tribunal)
Music industry

The deductibility of the acquisition cost of a licence in music rights has been a controversial issue. It resolves around whether such costs are entitled to depreciation (at the rate of 25 per cent on a written down value basis); or are in the nature of revenue expenditure, deductible in the first year or are to be amortised over the period of the licence. Various tribunals\(^2\) have held that the payment for acquiring music rights is in the nature of acquiring raw materials and hence, deductible as revenue expenditure.

Radio industry

Similar to music industry, radio broadcasters are also required to pay licence fees (a one-time entry fee and recurring annual fees) to the government as per the licence terms. The issue that has arisen is whether such fees, especially the one-time fees are in the nature of revenue expenditure to be claimed as deduction in the year in which they are incurred or are in the nature of capital expenditure, entitled to depreciation. One view is that the one-time entry fee could be allowable as a deduction over the period of licence. However, another view to this is that the payment for the one time entry fee could be treated towards licence acquisition, specifically covered as an intangible asset, eligible for depreciation at the rate of 25 per cent. This has resulted in disputes between the taxpayer and the tax authorities.

In addition to the above, the radio industry is also not very comfortable from a service tax perspective. Selling of space for advertisements in print media is part of the negative list of services and is currently, not subject to service tax\(^3\). Prior to 1 October 2014, this benefit was also available to other media such as out of home, internet, etc. However, the benefit was never granted to the radio industry.

Conclusion

Thus, whilst the industry is all set to march towards a high growth trajectory, the tax issues discussed above could act as a serious damper. There is an urgent need that the government clears up these issues by providing appropriate clarifications in the form of a circular or an amendment to the tax laws.

Also, it is pertinent to highlight that while the government is determined to introduce one of the biggest indirect tax reforms i.e. the GST regime, it should take care that the aforementioned indirect tax issues do not seep into the new tax environment to create ambiguities and confusions which could be the reason for probable litigations post its introduction.

(Note: This article includes inputs from FICCI – KPMG Indian Media and Entertainment Industry Report 2015 dated 24 March 2015.)

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2. Tips cassettes & Record Co. vs ACIT [2002] 82 ITD 641 (Mum Tribunal) and Tips cassettes & Record Co. vs ACIT [2002] 82 ITD 641 (Mum Tribunal) and Gramophone Co. of India Limited vs DCIT [1994] 48 ITD 145 (Calcutta Tribunal)

Regulatory updates

1. Withdrawal of five guidance notes on accounting by the ICAI

The Institute of Chartered Accountants of India (ICAI) has decided to withdraw five guidance notes on various accounting aspects as the same are no longer relevant in the present day context, in view of the requirements under the Companies Act, 2013 (the 2013 Act). The list of the guidance notes withdrawn are as follows:
   I. GN(A) 3 (Issued in 1982) - Guidance Note on Treatment of Reserve Created on Revaluation of Fixed Assets
   II. GN(A) 7 (Issued in 1989) - Guidance Note on Accounting for Depreciation in Companies
   III. GN (A) 8 (Issued in 1994) - Guidance Note on Some Important Issues Arising from the Amendments to Schedule XIV to the Companies Act, 1956
   IV. GN (A) 26 (Issued in 2008) - Guidance Note on the Applicability of Accounting Standard (AS) 20, Earnings Per Share
   V. GN (A) 27 (Issued in 2008) - Guidance Note on Remuneration Paid to Key Management Personnel - Whether a Related Party Transaction.

(Source: ICAI announcement dated 21 October 2015)

2. The RBI issues a report of the working group on the implementation of Ind AS by banks

Background

On 29 September 2015, the Reserve Bank of India (RBI) through its Fourth Bi-monthly Monetary Policy Statement, 2015-16 informed its stakeholders that it has recommended to the Ministry of Corporate Affairs (MCA) a road map for the implementation of Ind AS for banks and Non-Banking Financial Companies (NBFCs) from 2018-19 onwards.

The RBI constituted a working group (under the chairmanship of Shri Sudarshan Sen) for the same.

New development

Recently, the RBI issued a report of the working group which portrays the potential issues with respect to the implementation of Ind AS (Ind AS 109, Financial Instruments in particular) by banks in India along with its recommendations to ease out the implementation process.

The working group adopted a consultative approach and outreach meetings were held with bankers to understand their issues and apprehensions with regard to Ind AS, especially in the context of the current accounting practices. The group also reviewed several extant RBI instructions and guidelines as well as the Ind AS notified by the MCA to identify potential issues in relation to Ind AS implementation.
Accordingly, the working group structured its recommendations into the following key areas with a focus on financial instruments:

- Classification and measurement of financial assets
- Classification and measurement of financial liabilities
- Hedge accounting and derivatives
- Fair value measurement
- Impairment of financial assets
- Presentation of financial statements and disclosure
- Derecognition, consolidation and other residuary issues.

The working group also devised formats for financial statements of banks under Ind AS and application guidance thereon which are comprised in the given annexures:

- Annexure I: Proposed third schedule to the Banking Regulation Act, 1949
- Annexure II: Suggested formats for notes to financial statements
- Annexure III: Application guidance for preparation of financial statements
- Annexure IV: Instrument wise comparison of valuation requirements
- Annexure V: List of RBI instructions that need review
- Annexure VI: Educational material by the Institute of Chartered Accountants of India (ICAI)
- Annexure VII: Legislative amendments
- Annexure VIII: Survey of international practices for presentation of financial statements.

(Source: Report of the Working Group on Implementation of Ind AS by Banks in India dated 20 October 2015 and KPMG IFRS Notes - The RBI issues a report of the working group on the implementation of Ind AS by banks dated 26 October 2015)

3. The IASB agrees on an effective date for the new Leases Standard

Background

The International Accounting Standards Board (IASB) and the Financial Accounting Standards Board (FASB) have been working towards a converged standard for accounting of leases that would bring most of the leases on the balance sheet. This joint project was intended to replace the current lease accounting requirements under IFRS and the U.S. GAAP. Accordingly, the IASB and the FASB issued a revised Exposure Draft (ED) on leases in May 2013 which proposed changes towards both lessee and lessor accounting. The boards received extensive feedback on their proposals, and have heard a broad range of views. Since March 2014, they have redeliberated on almost all aspects of the project.

In their March 2015 meeting, the IASB and the FASB decided to prepare non-converged ballot drafts of their new standards on lease accounting i.e. to proceed with different lease accounting models.

New development

The IASB expects to issue the new Leases Standard (IFRS 16) in December 2015.

In its final meeting in October 2015, the IASB agreed on the effective date of the proposed standard. IFRS 16, would be effective for accounting periods beginning on or after 1 January 2019. An early adoption would be permitted, provided the company has adopted IFRS 15, Revenue from Contracts with Customers.

The FASB will discuss the effective date of its version of the standard in November 2015.

While deciding the effective date, the IASB took into consideration the comments of the respondents to the ED which stated that a significant period of time would be required between publication of the new standard and its effective date, due to the costs and complexities involved in the application of the proposals of the ED.

Additionally, the IASB also addressed five issues identified during the drafting process, namely:

- Accounting for lease modifications: A lessee (and a lessor holding a finance lease) would account for a lease modification that extends the use of an underlying asset (lease term) as a continuation of the existing lease. Such a lease modification should not be accounted for as a separate new lease.

A lessee (and a lessor holding a finance lease) would treat a lease modification as a separate new lease only if:

- the modification increases the scope of the lease by adding the right to use one or more underlying assets, and
- the increase in consideration is commensurate with the increase in scope.

- Reassessment of the discount rate for floating interest rate leases: For a floating interest rate lease, a lessee would update the discount rate whenever the lease payments are updated because of a change in the interest rate used to determine those payments.

- Costs associated with returning an underlying asset at the end of a lease: A lessee would account for restoration obligations associated with a lease in accordance with IAS 37, Provisions, Contingent Liabilities and Contingent Assets. A lessee would include an initial estimate of costs to be incurred in the measurement of the right-of-use asset, and would account for any changes in the obligation as an adjustment to the carrying amount of the right-of-use asset in accordance with IFRIC 1, Changes in Existing Decommissioning, Restoration and Similar Liabilities.

- The treatment of short-term leases and leases of low-value assets in a business combination: IFRS 3, Business Combinations should not require an acquirer to recognise assets or liabilities for short-term leases and leases of low-value assets in which the acquiree is the lessee.

- Required disclosures for leases that are part of a disposal group that is held for sale or discontinued operation: A lessee would not provide any disclosures for leases within the scope of IFRS 5, Non-current Assets Held for Sale and Discontinued Operations beyond those required by that standard.

(Source: KPMG IFRS Notes - The IASB agrees on an effective date for the new Leases Standard dated 27 October 2015)
4. SEBI prescribed format of uniform listing agreement and Business Responsibility Report

The Securities and Exchange Board of India (SEBI) on 2 September 2015 notified the SEBI (Listing Obligations and Disclosure Requirements) Regulations, 2015 (Listing Regulations). The SEBI has consolidated its detailed regulations covering listing obligations of various types of securities relating to different segments of the capital market. Further, through its circular dated 13 October 2015, it has issued a simplified listing agreement which is uniform across all types of securities/listed entities.

The requirement of executing a listing agreement by listed entities with the stock exchange is specified under different regulations related with the initial issuance of capital, as issued by SEBI. In order to give effect to the requirements of various regulations, SEBI has prescribed a specific format of the listing agreement. The listing agreement requires listed entities to submit company specific information and details of its securities with the stock exchange in the prescribed format. Listed entities are also required to intimate stock exchange of any change in information/details disclosed by them.

This listing agreement is a two page shortened version of the listing agreement as stated by SEBI in its press release dated 3 September 2015. A listed entity which has previously entered into agreement(s) with a recognised stock exchange(s) to list its securities should execute a fresh listing agreement with such a stock exchange within six months of the date of notification of the Listing Regulations.

Pursuant to notification of the Listing Regulation, Clause 34(2)(f) requires a Business Responsibility Report (BRR) for the top 100 listed entities based on market capitalisation (calculated as on 31 March every year). The BRR should describe the initiatives taken by such entities from an environmental, social and governance perspective, in the format as specified by SEBI from time to time.

Further, on 4 November 2015 through circular CIR/CFD/CMD/10/2015, SEBI has prescribed the format for a BRR to be submitted to the stock exchange. The circular further states that those listed entities which have been submitting sustainability reports to overseas regulatory agencies/stakeholders based on internationally accepted reporting frameworks need not prepare a separate report for the purpose of the above mentioned guidelines but only furnish the same to their stakeholders along with the details of the framework under which their BRR has been prepared and a mapping of the principles contained in these guidelines to the disclosures made in their sustainability reports.

The above mentioned circulars would come into force with effect from 90 days from notification of the Listing Regulations.


5. Risk management and interbank dealings: Booking of forward contracts - Liberalisation

As per Regulation 4 of the Foreign Exchange Management (Foreign exchange derivative contracts) Regulations, 2000, a person who is a resident in India may enter into a foreign exchange derivative contract to hedge an exposure to risk in respect of a transaction permissible under the Act/rules/regulations/directions/orders made or issued thereunder subject to the conditions specified in Schedule I of the regulations. The primary condition specified in Schedule I is verification by the authorised dealer of the documentary evidence produced by the person resident in India in order to ensure genuineness of the underlying exposure.

The RBI through its circular dated 29 October 2007 provided that resident individuals can manage/hedge their foreign exchange exposures arising out of actual or anticipated remittances, both inward and outward and are allowed to book forward contracts, without production of underlying documents, up to a limit of USD100,000 based on self-declaration.

The said limit of USD100,000 was further increased to USD250,000 through a notification dated 7 April 2014.

Recently, the RBI further increased this limit and provided that all resident individuals, firms and companies, who have actual or anticipated foreign exchange exposures are permitted to book foreign exchange forward contracts and foreign currency INR options contracts up to USD1,000,000 on the basis of a simple declaration and without the requirement of any kind of documentation.

(Source: Circular no. RBI/2015-16/201 dated 8 October 2015 by the RBI)

6. RBI mandated annual return on foreign liabilities and assets by LLPs

Background

The RBI requires that all Indian companies which have received Foreign Direct Investments (FDI) and/or have made FDI abroad in the previous year(s) including the current year, should file their annual return on Foreign Liabilities and Assets (FLA) with it in the soft form by 15 July each year.

Recent development

The RBI through its circular A.P (DIR Series) Circular No. 22 dated 21 October 2015 mandated that all Limited Liability Partnerships (LLPs) that have received FDI and/or have made FDI abroad (i.e. an overseas investment) in the previous year(s) as well as in the current year, should submit their FLA return to the RBI by 15 July each year, in the format as prescribed in the A.P (DIR Series) Circular No. 145 dated 18 June 2014.

The requirement came in with a view to capture the statistics relating to FDI, both inward and outward, by LLPs.

7. The MCA amends rules related to LLPs


Current guidance

Presently, for the purposes of satisfying the requirements of the proviso to Sub-section (1) of Section 58 of Limited Liability Partnership Act 2008, every firm, private company or unlisted public company which has been converted into a limited liability partnership, should make an intimation of such a conversion to the concerned Registrar of firms or Registrar of Companies (ROC), as the case may be, and should give details about the conversion and the particulars of the LLP in Form 14 (as prescribed in LLP Rules 2009) within 15 days of the date of registration of the LLP.

Amendment to the Rules

Under the amended rules, a private company or an unlisted public company which has been converted into a LLP are not required to file Form 14 with the ROC.

Thus, the amended rules have removed the requirement of filing an intimation of conversion to a LLP by companies to the ROC.

(Source: MCA notification dated 15 October 2015)

8. The MCA extends the last date for filing of the financial statements forms

Form for filing an annual return (MGT-7)

Section 92(4) of the 2013 Act requires that every company should file with the ROC, a copy of its annual return within 60 days from the date on which the Annual General Meeting (AGM) is held.

Rule 11(1) of the Companies (Management and Administration) Rules, 2014 requires that every company should prepare its annual return in the Form MGT-7.

Form for filing financial statements (AOC-4/AOC-4 XBRL)

Section 137 of the 2013 Act requires that every company should file with the ROC the following items:

- a copy of the financial statements, including Consolidated Financial Statements (CFS), if any.
- documents which are required to be attached with such financial statements under the 2013 Act, that have been duly adopted at the AGM of the company.

The above items should be filed with the ROC within 30 days of the date of the AGM with such fees and additional fees as may be prescribed in the 2013 Act.

Rule 12(1) of the Companies (Accounts) Rules, 2014 requires that every company should file the financial statements with the ROC together with Form AOC-4. Rule 12(2) provides that the class of companies notified by the central government should mandatorily file their financial statements in the eXtensible Business Reporting Language (XBRL) format and that the central government may specify the manner of filing under such a notification for such class of companies.

On 13 July 2015, the MCA issued a general circular no. 10/2015 where it has clarified that

- 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.

On 28 October 2015, in continuation to the above mentioned circular, the MCA has further relaxed that Forms AOC-4, AOC-4 XBRL and MGT-7 can be filed with the ROC upto 30 November 2015, without payment of additional fees.

(Source: General Circular No 10/2015 dated 13 July 2015 and General Circular No. 14/2015 dated 28 October 2015 and KPMG First Notes: The MCA extends the last date for filing of annual return and financial statements forms dated 14 July 2015)
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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.

ICAI releases revised guidance on Internal Financial Controls Over Financial Reporting

16 September 2015

Background

The Institute of Chartered Accountants of India (ICAI) had issued a Guidance Note in November 2014. This guidance note was revised subsequently and the ICAI issued a revised ‘Guidance Note on Audit of Internal Financial Controls Over Financial Reporting’ (Guidance Note) on 14 September 2015.

Our First Notes provides an overview of the Guidance Note issued by ICAI.

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

Previous editions are available to download from: www.kpmg.com/in

Lost an issue of Accounting and Auditing Update or First Notes?

The IASB agrees on an effective date for the new Leases Standard

27 October 2015

Background

The International Accounting Standards Board (IASB) and the Financial Accounting Standards Board (FASB) have been working towards a converged standard for accounting for leases that would bring most leases on-balance sheet. This joint project was intended to replace the current lease accounting requirements under IFRS and U.S. GAAP. Accordingly, the IASB and the FASB issued a revised Exposure Draft (ED) on leases in May 2013 which proposed changes towards both lessee and lessor accounting. The boards received extensive feedback on their proposals, and have heard a broad range of views. Since March 2014, they have redeliberated on almost all aspects of the project.

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New developments

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