Guide to First-time Adoption of Ind AS
## Contents

<table>
<thead>
<tr>
<th>Section</th>
<th>Page</th>
</tr>
</thead>
<tbody>
<tr>
<td>Overview of Ind AS roadmap</td>
<td>06</td>
</tr>
<tr>
<td>Key differences between Ind AS and Indian GAAP</td>
<td>10</td>
</tr>
<tr>
<td>First-time adoption of Ind AS</td>
<td>42</td>
</tr>
<tr>
<td>Ind AS conversion challenges and perspectives</td>
<td>84</td>
</tr>
<tr>
<td>Appendix: Sample Ind AS reconciliation note for first Ind AS financial statements</td>
<td>98</td>
</tr>
</tbody>
</table>
The transition from Indian GAAP to Ind AS is a historic and a landmark change. In accordance with its commitment to G20, India is converging to IFRS in a phased manner starting from annual periods beginning on or after 1 April 2016. The IFRS converged standards will be known as Indian Accounting Standards (Ind-AS) and will contain numerous carve outs from IFRS. The change to Ind AS is a hugely positive move that will bring the accounting in India substantially closer to the accounting followed by the global companies under IFRS.

Due to carve outs, Indian companies may not be able to make a dual statement of compliance with both Ind AS and IASB IFRS. Therefore, Indian companies may not be able to use Ind AS financial statements for global listing purposes that require compliance with IFRS. However, Indian companies may find it easier to prepare IFRS financial statements from Ind AS financial statements rather than Indian GAAP financial statements.

The application of Ind AS is more than a mere accounting or technical exercise. The consequences are far wider than financial reporting issues, and extend to various significant business and regulatory matters including debt covenants, dividend, managerial remuneration, ESOP, minimum alternate tax (MAT), training of employees, IT systems, internal control and taxation. A case in point is infrastructure companies. They may have to pay higher MAT, if MAT is based on Ind AS profits, because under Ind AS, construction revenue and profits are recognized upfront in a service concession arrangement. As a CBDT committee is still examining these issues, companies must engage with these agencies to put their concerns at the forefront. It is imperative that companies identify and address these and many other issues in their Ind AS conversion project.

Ind AS conversion will not be a hassle-free job. At the same time, with appropriate planning and an early start, it may not be a hugely painful exercise. Experience tells us that major European companies took about eighteen months to two years to convert from national GAAP to IFRS. Our recommendation to entities in phase 1 and 2, that have not started the process of Ind AS conversion is to start immediately. More importantly, there are no disadvantages to getting a start on the process, but the advantages include:

- Securing the right people, whether by engaging a third party to provide assistance or by hiring them directly
- Putting fewer burdens on valuable accounting, financial reporting and IT resources as the conversion date nears
- More time to train employees on Ind AS and to make them comfortable with the standards and interpretations, and
- Discussing the financial reporting effects of conversion to Ind AS with investors and analysts to provide them with some sense of the changes in financial statements due to the new framework.

This publication will provide entities a head start on Ind AS and answer questions such as the following:

- What are the major differences between Ind AS and Indian GAAP?
- How to convert Indian GAAP balance sheet to Ind AS balance sheet on first time adoption?
- How will Ind AS impact the financial statements of entities and what would be the conversion efforts?
- What challenges, other than converting the financial statements, should entities prepare themselves for?
- What approach or strategy should be followed in transiting to Ind AS?

The next few years will be exciting, but challenging at the same time. We are committed to help you migrate to Ind AS as smoothly as possible, and look forward to teaming with you on this landmark journey.

We will be happy to receive your feedback and answer any questions that you may have.

Best wishes,

Ernst & Young LLP
Overview of Ind AS roadmap

On 16 February 2015, the Ministry of Corporate Affairs (MCA) notified the Companies (Indian Accounting Standards) Rules, 2015 laying down the roadmap for application of IFRS converged standards (Ind AS) to Indian companies other than banking companies, insurance companies and non-banking finance companies (NBFCs). The Government has also notified Ind AS standards (known as ‘Indian Accounting Standards) for application by these companies.

- Voluntary Phase: Early adoption of Ind AS is permitted from financial year beginning on or after 1 April 2015.

- Mandatory Phase 1: Application of Ind AS is mandatory from the financial year beginning on or after 1 April 2016, for the following companies:
  - Listed or non-listed companies with net worth of INR500 crores (INR5 billion) or more
  - Holding, subsidiaries, joint ventures or associates companies of these companies

- Mandatory Phase 2: Application of Ind AS is mandatory from the financial year beginning on or after 1 April 2017, for the following companies:
  - All listed companies not covered under the mandatory phase 1
  - Non-listed companies with net worth of INR250 crores (INR2.5 billion) or more and not covered in the mandatory phase 1
  - Holding, subsidiaries, joint ventures or associates of these companies
  - All companies applying Ind AS are required to present comparative information according to Ind AS for one year. This requires companies to start applying Ind AS from the beginning of the previous period. For example, a company covered under mandatory phase 1 needs to apply Ind AS for financial year beginning on or after 1 April 2016. In addition, it also needs to give Ind AS comparatives for the year ended 31 March 2016. Consequently, its needs to start applying Ind AS from 1 April 2015.
  - Ind AS will apply to both standalone financial statements (SFS) and consolidated financial statements (CFS) of companies covered under the roadmap.
  - Companies not covered under the roadmap can either apply Ind AS voluntarily or continue applying existing standards, i.e., accounting standards notified under the Companies (Accounting Standards) Rules 2006 (as amended) (hereinafter referred to as “current Indian GAAP”).
Any company opting to apply Ind AS will need to prepare its financial statements according to Ind AS consistently. Once Ind AS are applied voluntarily, this option will be irrevocable and such companies will not be required to prepare another set of financial statements in accordance with current Indian GAAP.

Net worth for a company is to be calculated in accordance with its SFS as on 31 March 2014 or the first audited financial statements for accounting period which ends after that date. Accordingly, if a company has net worth more than INR500 crores (INR5 billion) as of 31 March 2015, then it will be covered in the Phase 1 itself and apply Ind AS from financial year beginning on or after 1 April 2016.

Insurance companies, banking companies and NBFCs will not be required to apply Ind AS for preparation of their financial statements either voluntarily or mandatorily.

The adoption of Ind AS in accordance with the roadmap will bring accounting in India closer to the world at large that has adopted/converged with IFRS. India has gone for the Convergence approach instead of full adoption of IFRS as issued by the International Accounting Standards Board (IASB). Ind AS contains certain changes vis-à-vis IASB IFRS. Consequently, financial statements prepared in accordance with Ind AS may not be fully compliant with IASB IFRS.

Given below are salient features of Ind AS roadmap notified by the MCA:

<table>
<thead>
<tr>
<th>Phase 1</th>
<th>2015-16</th>
<th>2016-17</th>
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<tr>
<td>April</td>
<td>April</td>
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<tr>
<td>March</td>
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<tr>
<td>Opening Balance Sheet 1 April 2015</td>
<td>Comparative for 31 March 2016</td>
<td>Financial statements for year ended 31 March 2017</td>
</tr>
</tbody>
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<tr>
<th>Phase 2</th>
<th>2016-17</th>
<th>2017-18</th>
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<tbody>
<tr>
<td>April</td>
<td>April</td>
<td>April</td>
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<td>March</td>
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<tr>
<td>Opening Balance Sheet 1 April 2016</td>
<td>Comparative for 31 March 2017</td>
<td>Financial statements for year ended 31 March 2018</td>
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Practical issues and perspective

Given below is an overview of practical issues that are expected to arise on the applicability of the Ind AS roadmap and our perspectives on these issues. It is expected that the Ministry of Corporate Affairs (MCA) or the Institute of Chartered Accountants of India (ICAI) may provide guidance on these issues.

1. **Ind AS roadmap prescribes applicability based on financial years beginning on or after 1 April.** Given below is the first Ind AS applicability date under various phases for companies not having a 31 March year-end:

<table>
<thead>
<tr>
<th>Year-end</th>
<th>Voluntary Phase</th>
<th>Mandatory Phase 1</th>
<th>Mandatory Phase 2</th>
</tr>
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<tbody>
<tr>
<td>31 December</td>
<td>1 January 2016</td>
<td>1 January 2017</td>
<td>1 January 2018</td>
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<tr>
<td>30 June</td>
<td>1 July 2015</td>
<td>1 July 2016</td>
<td>1 July 2017</td>
</tr>
<tr>
<td>30 September</td>
<td>1 October 2015</td>
<td>1 October 2016</td>
<td>1 October 2017</td>
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Companies are also required to present comparative information according to Ind AS for one year.

2. **The Companies Act, 2013 (the “Act”) requires that all companies, except those exempted by the Tribunal, should have 31 March year-end.** A company needs to consider this aspect carefully along with Ind AS applicability dates to decide the financial year from which it is allowed/required to start applying Ind AS. Consider that XYZ Limited has net worth exceeding INR500 crores (INR5 billion). It has historically used calendar year (i.e., 12 month period ending 31 December) as its financial year. To comply with the Act’s requirements concerning uniform financial year, it is preparing financial statements for the 15-month period from 1 January 2015 to 31 March 2016. Since Ind AS applicability is decided based on the beginning of the financial year and not the end, XYZ cannot apply Ind AS in its financial statements for the year ended 31 March 2016, either mandatorily or voluntarily. However, since XYZ has net worth exceeding INR500 crores (INR5 billion), it will start applying Ind AS from financial year beginning 1 April 2016. The first Ind AS financial statements of XYZ will have comparative information for 15-month periods, i.e., from 1 January 2015 to 31 March 2016. Its date of transition to Ind AS will be 1 January 2015.

3. **The roadmap requires companies to apply either Ind AS or existing accounting standards in entirety.** Companies are not allowed to adopt standards by mix and match or slicing and dicing. However, current Indian GAAP does not prescribe specific accounting for various transactions, other events or conditions. For example, current Indian GAAP does not contain comprehensive accounting for service concession arrangements. We believe that a company applying current Indian GAAP can refer to Ind AS for accounting of service concession arrangements, to the extent that Ind AS accounting does not contradict with the principles under Indian GAAP.

4. **In accordance with the roadmap, Ind AS also applies to holding, subsidiary, joint venture and associates of companies meeting Ind AS applicability criteria.** The roadmap does not define these terms. It merely states that “words and expressions used herein and not defined in these rules but defined in the Companies Act shall have the same meaning respectively assigned to them in the Companies Act”. Our view is that definitions according to Ind AS should be used due to the following key reasons:

   a) Ind AS are contained in the Annexure to the Companies (Indian Accounting Standards) Rules, 2015. Hence, they are part of the rules/roadmap. The roadmap requires definitions according to the Act to be applied only if they are not defined in the roadmap itself.

   b) The Act has defined the term mainly from regulatory purposes. For accounting purposes, definitions according to applicable accounting standards are applied.

   c) The roadmap requires holding, subsidiaries, joint ventures and associates of companies meeting Ind AS applicability criteria to adopt Ind AS from the same date to facilitate the preparation of CFS. The application of this view ensures that this objective is met in its true spirit.
5. The roadmap requires that, to decide Ind AS applicability, net worth should be computed according to section 2(57) of the Act. The section defines the term as below:

“Net worth means the aggregate value of the paid-up share capital and all reserves created out of the profits and securities premium account, after deducting the aggregate value of the accumulated losses, deferred expenditure and miscellaneous expenditure not written off, as per the audited balance sheet, but does not include reserves created out of revaluation of assets, write-back of depreciation and amalgamation.”

However, the roadmap is silent as to whether net worth to determine Ind AS applicability will be calculated in accordance with Indian GAAP or Ind AS. From practical perspective, a company will first decide the applicability and then start applying Ind AS. Hence, we believe that the net worth calculated in accordance with Indian GAAP should be used to determine the applicability of Ind AS. This view is also supported by the fact that a company needs to first assess Ind AS applicability as on 31 March 2014. Companies are not allowed to prepare Ind AS financial statements for the year ended 31 March 2014.

6. In accordance with the roadmap, insurance companies, banking companies and NBFCs are not required to apply Ind AS for preparation of their financial statements either voluntarily or mandatorily. We believe that companies in the financial services sector are not required to apply Ind AS for their own statutory reporting even if they are holding, subsidiary, joint venture or associates of companies in the non-financial services sector meeting Ind AS applicability criteria. For example, an NBFC is a subsidiary of the company covered in mandatory phase 1 of Ind AS adoption. The NBFC is not required to adopt Ind AS along with its non-financial sector parent company. Nor can the NBFC adopt Ind AS voluntarily for its statutory reporting at this stage. Similar principle applies even to banking and insurance companies. This is because the Reserve Bank of India (RBI) and the Insurance and Regulatory Development Authority (IRDA) have prescribed various accounting guidelines for banking companies, NBFCs and insurance companies, which are not in sync with Ind AS. Until RBI and IRDA do not adopt Ind AS and modify/withdraw their existing guidelines to align with Ind AS, banking and insurance companies and NBFCs cannot apply Ind AS for their own statutory reporting.

Ind AS 110 Consolidated Financial Statements is clear that a parent will prepare CFS using uniform accounting policies for like transactions and other events in similar circumstances. Moreover, it is a settled principle that all accounting policies used in the preparation of CFS should be compliant with the accounting standards under which CFS are prepared. As stated above, many aspects of RBI guidelines on accounting are not Ind AS compliant. Hence, the parent cannot use Indian GAAP financial statements of the NBFC for preparing its CFS. Rather, the NBFC will need to prepare Ind AS group reporting package to facilitate preparation of Ind AS CFS by the parent.

7. In accordance with Ind AS roadmap, the first Ind AS financial statements of a company should contain comparative figures for at least one year. Moreover, Ind AS 101 requires companies to prepare an Ind AS opening balance sheet at the transition date.

To obtain appropriate audit evidence regarding account balances and disclosures in the Ind AS financial statements for the current period, the auditor will also need to obtain sufficient appropriate audit evidence about the opening Ind AS balance sheet and Ind AS adjustments for the comparative period. As a result, audit procedures, which an auditor performs in relation to the comparative financial information, are likely to be more extensive than the work generally performed on comparative information. The auditor will also perform audit procedures on Ind AS reconciliations from the previous GAAP to Ind AS.
Revenue recognition

Key differences

Under Indian GAAP, revenue recognition is dealt with under AS 9 Revenue Recognition and AS 7 Construction Contracts. Ind AS 115 Revenue from Contracts with Customers is a single standard which deals with revenue recognition in a comprehensive manner under the Ind AS regime.

The application of Ind AS 115 will change the requirements for recognizing revenue for most companies, particularly for companies in the real estate and construction industry. IFRS 15 Revenue from Contracts with Customers is effective for IFRS reporting entities for the first interim period within annual reporting periods beginning on or after 1 January 2017, and will allow early adoption. Unlike IFRS, Ind AS requires immediate application of Ind AS 115 and does not provide a choice between IAS 18 Revenue/IAS 11 Construction Contracts and IFRS 15. This eliminates the need to convert twice, i.e., applying IAS 18/IAS 11 on first time adoption and later changing to IFRS 15 from 1 April 2017. Therefore, India will probably be the first country to apply IFRS 15, without any precedence or experience of its application in other countries. This may not be the best outcome, considering that IFRS 15 requires application of a significant amount of judgment, and there are many open interpretative issues that IASB and FASB have to resolve. Pending unresolved issues, IASB has recently proposed to defer the application of IFRS 15 for IFRS reporting entities by one year i.e., reporting periods beginning on or after 1 January 2018. Till the finalization of this publication, the ICAI has not issued any such proposal under Ind AS for public comment.

Ind AS 115 sets-out principles that an entity applies to report useful information about the amount, timing, and uncertainty of revenue and cash flows arising from its contracts to provide goods or services to customers. The core principle requires an entity to recognize revenue to depict the transfer of goods or services to customers in an amount that reflects the consideration that it expects to be entitled to in exchange for those goods or services.

Ind AS 115 applies to all contracts with customers, except for contracts that are within the scope of other standards, such as leases, insurance, and financial instruments. It is a comprehensive standard that deals with revenue recognition.

Ind AS 115 establishes the following five-step model that will apply to revenue earned from a contract with a customer (with limited exceptions), regardless of the type of revenue transaction or the industry.

1. Identify the contract(s) with a customer

Contracts may be written, verbal or implied by customary business practices, but must be enforceable and have commercial substance. The model applies to each contract with a customer once it is probable the entity will collect the consideration to which it will be entitled.
2. Identify the performance obligations in the contract
   A performance obligation is a promise (or a group of promises) that is distinct, as defined in the revenue standard. In certain cases, identifying performance obligations can be relatively straightforward, such as an electronics store's promise to provide a television. In many other cases, it can be more complex, such as a contract to provide a new computer system with a three-year software license, a right to upgrades, and technical support. Entities must determine whether to account for performance obligations separately, or as a group.

3. Determine the transaction price
   The transaction price is the amount of consideration an entity expects to be entitled to from a customer in exchange for providing goods or services. Several factors should be considered to determine the transaction price, including whether there is variable consideration, a significant financing component, non-cash consideration, or amounts payable to the customer.

4. Allocate the transaction price to the performance obligations in the contract
   The transaction price is allocated to separate performance obligations in the contract based on relative standalone selling prices. Determining the relative standalone selling price can be challenging when goods or services are not sold on a standalone basis. Ind AS 115 sets out several methods that can be used to estimate a standalone selling price when one is not directly observable. Allocating discounts and variable consideration must also be considered.

5. Recognize revenue when (or as) the entity satisfies a performance obligation
   Revenue is recognized when (or as) the performance obligations are satisfied. An entity satisfies a performance obligation by transferring control of a promised good or service to the customer, which could occur over time or at a point in time. A performance obligation is satisfied at a point in time unless it meets one of the following criteria, in which case, it is satisfied over time:
   - The customer simultaneously receives and consumes benefits provided by the entity's performance as the entity performs.
   - The entity's performance creates or enhances an asset that the customer controls as the asset is created or enhanced.
   - The entity's performance does not create an asset with an alternative use to the entity and the entity has an enforceable right to payment for performance completed to date.

Revenue is recognized in line with the pattern of transfer. Revenue that is allocated to performance obligations satisfied at a point in time will be recognized when control of the good or service underlying the performance obligation has been transferred. If the performance obligation is satisfied over time, the revenue allocated to that performance obligation will be recognized over the period the performance obligation is satisfied, subject to additional application guidance to assist entities when determining whether a license of intellectual property transfers to a customer over time or at a point in time.

Revenue is recognized when a customer obtains control of a good or service, i.e., when it has the ability to direct the use of and obtain the benefits from the good or service. This is different from the concept of transfer of risks and rewards espoused in AS 9. It is also different from the current concept of recognizing revenue as the earnings process is completed. Companies will also need to determine if there is a continuous transfer of control and consequently whether revenue should be recognized over time or at a point in time.

Application guidance is provided in Ind AS 115 to assist entities in applying its requirements to common arrangements, including: licenses; warranties; rights of return; principal-versus-agent considerations; options for additional goods or services and breakage.
Contract costs and other application guidance

In addition to the five-step model, Ind AS 115 specifies how to account for the incremental costs of obtaining a contract and the costs directly related to fulfilling a contract. Provided those costs are expected to be recovered, they can be capitalized and subsequently amortized and tested for impairment.

Time value of money

Some contracts with the customer may contain significant financing element, either explicitly or implicitly. When the financing element is significant, an entity should adjust the transaction price for the time value of money. Ind AS 115 provides certain exceptions to applying this guidance and a practical expedient, which allows entities to ignore time value of money if the time between transfer of goods or services and payment is less than one year.

Disclosures

Extensive disclosures are required to provide increased insight into both revenue that has been recognized, and revenue that is expected to be recognized in the future from existing contracts. Quantitative and qualitative information will be provided about the significant judgments and changes in those judgments that management made to determine revenue that is recorded.

Key impact

Key challenges in applying five-step model

The application of five-step models in Ind AS 115 gives rise to various practical challenges. The following diagram provides an overview of key challenges that are expected to arise.

Multiple element arrangements

According to AS 9, revenue is measured by the charge made to customers for goods supplied and services rendered and by the charges and rewards arising from the use of resources by them. Under Indian GAAP, an Expert Advisory Committee (EAC) opinion deals with accounting for multiple element contracts in a limited manner. In the absence of specific guidance, it sometimes becomes difficult to determine revenue for a contract that contains multiple elements such as sale of goods and rendering of services. In contrast, Ind AS 115 prescribes that the transaction price in such arrangements must be allocated to each separate performance obligation, so that revenue is recorded at the right time and for the right amount.

Control model

Ind AS 115 has introduced the control model to determine the point of revenue recognition. Management needs to determine, at contract inception, whether control of a good or service transfers to a customer over time or at a point in time. Arrangements where the performance obligations are satisfied over time are not limited to services arrangements. Complex assets or certain customized goods constructed for a customer, such as a complex refinery or specialized machinery, could also be transferred over time, depending on the facts and circumstances. Revenue is recognized over time if prescribed criteria are met. This model may have significant impact on companies engaged in construction or real estate business.
**Financial instruments**

Ind AS 109 *Financial Instruments*, Ind AS 32 *Financial Instruments: Disclosures* and Ind AS 113 *Fair Value Measurement* deal with presentation, recognition, measurement and disclosure aspects of financial and equity instruments in a comprehensive manner. Pronouncements that deal with certain types of financial instruments under Indian GAAP are AS 11 *The Effects of Changes in Foreign Exchange Rates*, AS 13 *Accounting for Investments* and the ICAI Announcement on Accounting for Derivatives.

Recently, the ICAI has issued the *Guidance Note on Accounting for Derivative Contracts*. This Guidance Note applies to all entities that do not apply Ind AS. The Guidance Note deals with recognition, measurement, presentation and disclosure for derivative contracts. The Guidance Note also deals with accounting for derivatives where the hedged item is covered under notified Accounting Standards, e.g., a commodity, an investment, etc. The Guidance Note, however, does not cover accounting for foreign exchange forward contracts, which are within the scope of AS 11. This Guidance Note is applicable for financial year beginning on or after 1 April 2016. Its earlier application is permitted.

**Key differences**

- Ind AS 32 establishes detailed principles for presenting financial instruments as liabilities or equity. One key feature, which requires a financial instrument to be classified as a liability, is the existence of a contractual obligation of one party (the issuer) to deliver cash or another financial asset to another party (the holder), or to exchange financial assets or liabilities under conditions that are potentially unfavorable. In contrast, in the case of an equity instrument, the issuer has no obligation to deliver cash or another financial asset to the holder of the instrument. The application of these principles requires certain instruments that have the form of equity to be classified as liability. For example, under Ind AS 32, mandatorily redeemable preference shares on which a fixed dividend is payable are treated as a liability. Under Indian GAAP, notified accounting standards do not prescribe distinction between equity and liabilities. Essentially, classification and accounting for liability and equity is dictated by the legal form of the instrument.

- Ind AS 32 requires compound financial instruments, such as convertible bonds, to be split into liability and equity components, and each component is recognized separately. The current Indian GAAP does not entail split accounting, and financial instruments are classified as either a liability or equity, depending on their primary nature. For example, under current Indian GAAP, a convertible debenture is generally treated as liability in entirety.

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1  *IFRS 113 Fair Value Measurement* consolidates fair value measurement guidance from across various IFRS into a single standard. It does not change when fair value can or should be used.
Under Ind AS 109, all financial assets are classified among three principal categories, namely, measured at amortized cost, fair value through other comprehensive income (FVTOCI) and fair value through profit or loss (FVTPL). “Amortized cost” measurement is applicable only for “debt instruments.” An entity may be able to use FVTPL and FVTOCI categories both for debt and equity instruments. The following diagram explains the classification requirements.

A financial asset is subsequently measured at amortized cost only if – (i) the asset is held within a business model whose objective is to collect contractual cash flows, and (ii) the contractual terms of the financial asset give rise to cash flows that are solely the payments of principal and interest (SPPI). A financial asset is subsequently measured at FVTOCI if it (i) meets the SPPI criterion, and (ii) is held in a business model whose objective is achieved by both collecting contractual cash flows and selling financial assets. All other financial assets are classified as being subsequently measured at FVTPL. For equity investments that are not held for trading, an entity may irrevocably elect at initial recognition to present subsequent changes in the fair value in OCI.

Under Indian GAAP, loans and receivables are typically measured at cost, less provision for doubtful debts. Interest income on loans is recognized on time-proportion basis at rates mentioned in the loan agreement. AS 13 requires an investment to be classified either as long-term or current investment. After initial recognition, long-term investments are measured at cost, less than temporary diminution in the value of investment. Interest, if any, is recognized on time proportion basis. Current investments are measured at lower of cost or market price.

Under Ind AS 109, all financial liabilities are classified either as at FVTPL or amortized cost. Financial liabilities are classified as at FVTPL when they meet the definition of held-for-trading, or when they are designated as such on initial recognition. An entity may designate a financial liability as at FVTPL only if it meets prescribed criteria at its initial recognition. Initial measurement of all financial liabilities is at fair value. Subsequent to initial recognition, FVTPL liabilities are measured at fair values, with gain or loss normally being recognized in profit or loss. For non-derivative financial liabilities that are designated for measurement as at FVTP, the element of gain or loss attributable to changes in credit risk should normally be recognized in equity and the remainder is recognized in profit or loss. All other financial liabilities are measured at amortized cost using the effective interest rate method.

Ind AS 109 requires an entity to decide classification of financial liabilities on initial recognition. No subsequent reclassification of financial liabilities is allowed.

The diagram given below explains the classification requirements:

![Classification of financial liabilities diagram](image-url)
Under Indian GAAP, accounting standards do not provide detailed guidance on measurement of financial liabilities. The common practice is to recognize a financial liability at the consideration received on its recognition. Subsequently, interest is recognized at a contractual rate, if any.

- Ind AS 109 defines a derivative as a financial instrument or other contract with the following three characteristics:
  - Its value changes in response to the change in a specified interest rate, financial instrument price, etc.
  - It requires zero or smaller initial net investment.
  - It is settled at a future date.

According to Ind AS 109, all derivatives are measured at fair value and any gains/losses, except gains/losses on derivatives used for hedge purposes, are recognized in profit or loss.

Under Indian GAAP, AS 11 deals with foreign currency forward exchange contracts (except for those entered into, to hedge a firm commitment or highly probable forecast transaction). Accounting prescribed under AS 11 for such forward contracts is based on whether the contract is for hedge or speculation purposes. For derivatives not covered under AS 11, the ICAI Announcement on Accounting for Derivatives requires a mark-to-market loss to be provided for open derivative contracts as on the balance sheet date. Mark-to-market gains generally remain outside the balance sheet. Alternatively, the company may apply principles of AS 30 Financial Instruments: Recognition and Measurement to derivatives whose accounting is not covered under AS 11. According to AS 30, all derivatives are measured at fair value, and any gains/losses, except gains/losses on derivatives used for hedge purposes, are recognized in profit or loss.

As stated above, the ICAI has recently issued the Guidance Note on Accounting for Derivative Contracts, which is applicable from financial years beginning on or after 1 April 2016. The Guidance Note requires that all derivatives are measured at fair value, and any gains/losses, except gains/losses on derivatives used for hedge purposes, are recognized in profit or loss.

- Ind AS 109 does not permit embedded derivatives to be separated from host contracts that are financial assets. Rather, an entity applies Ind AS 109 classification requirements to the entire hybrid contract. In case of all other contracts, Ind AS 109 requires that an embedded derivative should be separated from the host contract and accounted for as a derivative if, and only if:
  a) The economic characteristics and risks of the embedded derivative are not closely related to the economic characteristics and risks of the host contract,
  b) A separate instrument with the same terms as the embedded derivative will meet the definition of a derivative, and
  c) The hybrid (combined) instrument is not measured at fair value with changes in fair value recognized in the statement of profit and loss (i.e., a derivative that is embedded in a financial liability at fair value through profit or loss is not separated).

Under Indian GAAP, notified accounting standards do not contain specific guidance on embedded derivatives. Typically, entities do not identify embedded derivatives separately.

- Ind AS 109 deals with various aspects of hedge accounting in a comprehensive manner. It defines three types of hedging relationships, namely, fair value hedges, cash flow hedges and hedges of net investments in a foreign operation. It also lays down prerequisite conditions to apply hedge accounting.

Under Indian GAAP, AS 11 deals with forward exchange contracts for hedging foreign currency exposures (except for those arising from firm commitments or highly probable forecast transactions). There is no mandatory accounting standard for other types of hedge. However, the Guidance Note on Accounting for Derivative Contracts applicable from financial years beginning on or after 1 April 2016 contains detailed principles for hedge accounting, which are similar to Ind AS 109.

- Ind AS 109 introduces a new “expected credit loss (ECL) model” for impairment of financial assets. The new model applies to financial assets that are not measured as at FVTPL, including loans, leases and trade receivables, debt securities, contract assets under Ind AS 115 and specified financial guarantees and loan commitments issued. The new model does not apply to equity instruments, since they are carried at FVTOCI. The model uses a dual measurement approach, under which the loss allowance is measured as either 12 month expected credit losses (ECL) or lifetime expected credit losses (lifetime ECL). To determine the application of 12-month ECL vs. lifetime ECL, an entity must determine whether there has been a significant increase in credit risk since the initial recognition of an asset. If credit risk has not increased significantly, 12-month ECL is used to provide for impairment loss. However, if credit risk has increased significantly, lifetime ECL is used.
Under the current Indian GAAP, there is no detailed guidance on methodology for determining the impairment of financial assets, such as loan and receivables.

Ind AS 109 deals with derecognition of financial assets in a comprehensive manner. Ind AS 109 derecognition rules for financial assets are extremely complex. The decision whether a transfer qualifies for derecognition is made by applying a combination of risk and rewards and control tests. The use of two models often create confusion, however, those have been addressed by ensuring that the risk and rewards test is applied first, with the control test used only when the entity has neither transferred substantially all risks and rewards of the asset nor retained them. Derecognition cannot be achieved by only a legal transfer. The transfer has to happen in substance, which is evaluated by using a risk and rewards and a control model. A legal opinion from a qualified attorney is normally required to conclude on highly complex issues.

Under Indian GAAP, notified accounting standards do not deal with derecognition of financial assets/liabilities in a comprehensive manner. There is no accounting standard dealing with consolidation of special purpose entities (SPEs). Consequently, differing practices are prevalent with regard to derecognition of financial assets and liabilities. It is understood that under Indian GAAP, many entities may derecognize financial assets transferred under the arrangements, such as, bill discounting and/or factoring of trade receivables, from their Indian GAAP financial statements. This is despite the fact that the transferor may have provided credit enhancements to the transferee.

Ind AS 109 provides detailed guidance on derecognition of a financial liability. An entity derecognizes a financial liability or a part of it from the balance sheet when, and only when, it is extinguished. A liability is extinguished when the obligation specified in the contract is discharged, cancelled or expires. Ind AS 109 requires an exchange between an existing borrower and lender of debt instruments with “substantially different” terms to be accounted for as an extinguishment of the original financial liability and the recognition of a new financial liability. Similarly, a substantial modification of the terms of an existing financial liability, or a part of it, (whether or not due to the financial difficulty of the debtor) should be accounted for as an extinguishment of the original financial liability and the recognition of a new financial liability.

In accordance with Ind AS 109, the terms of exchanged or modified debt are regarded as ‘substantially different’ if the net present value of the cash flows under the new terms (including any fees paid net of any fees received) discounted at the original EIR is at least 10% different from the discounted present value of the remaining cash flows of the original debt instrument. In addition, there may be a situation where the modification of the debt is so fundamental that immediate derecognition is appropriate whether or not the ‘10% test’ is satisfied.

Under the current Indian GAAP, there is no detailed guidance on determining derecognition of financial liabilities.

Ind AS 107 requires entities to provide comprehensive disclosures in their financial statements to enable users to evaluate:

- The significance of financial instruments for its financial position and performance, and
- The nature and extent of risks arising from financial instruments, and how the entity manages those risks.

The disclosures required under Ind AS 107 include quantitative and qualitative information.

Under Indian GAAP, ICAI has issued an Announcement on Disclosure regarding Derivative Instruments, which requires certain minimum disclosures to be made concerning financial instruments. However, the Guidance Note on Accounting for Derivative Contracts applicable from financial years beginning on or after 1 April 2016 requires more comprehensive disclosures with regard to derivative instruments and hedge accounting.

Ind AS 113 defines fair value, provides principles-based guidance on how to measure fair value and requires information about those fair value measurements to be disclosed. It provides a framework to reduce inconsistency and increase comparability in fair value measurements used in financial reporting. It does not address the question of which assets or liabilities are to be measured at fair value or when those measurements must be performed. An entity must look to other standards in that regard. The standard applies to all fair value measurements, when fair value is required or permitted by Ind AS, with limited exceptions.

The current Indian GAAP does not contain detailed guidance on methodology for fair value measurements.
Key impact

Liability v. equity classification

Due to application of Ind AS 109, liability and equity classifications of financial instruments may change substantially. Some of the instruments, such as redeemable preference shares, are classified as equity under the current Indian GAAP. Under Ind AS, these may be identified as liabilities, either wholly or partly. Similarly, on adoption of Ind AS, compound instruments will need to be split between debt and equity component. Each portion is then treated separately.

The accounting classification of an instrument as a liability or equity is much more than an accounting matter or matter of presentation in financial statements. Particularly, it may have significant impact on reported financial performance of an entity. For instance, if an instrument needs to be classified as liability instead of equity, any return payable thereon will be charged to profit or loss as expense, instead of distribution of profit. Moreover, such change in classification will impact key performance indicators such as debt-equity ratio, interest coverage ratio, debt service ratio and earnings per share. This in turn, is likely to impact decision making of stakeholders such as financial institutions, investors, vendors, customers and tax authorities. It could also result in non-compliance with debt covenants, and could affect other amounts such as the number of stock options to be granted or managerial remuneration to be paid.

It is not necessary that Ind AS 32 will only have a negative impact. Depending on the situation of each company and the nature of instruments issued, the impact could either be positive or negative. For example, certain reputed companies have issued perpetual bonds to raise long-term financing. As the name suggests, these bonds do not have any fixed maturity. These bonds, therefore, give a comfort of equity to the issuer. At the same time, the issuer, at its discretion, may redeem these bonds at a later date. Based on the exact legal and contractual terms of perpetual bonds, it may be possible to conclude that these bonds are not liability for the issuer; rather, they are part of equity under Ind AS. If so, the issuer will treat interest payable on these bonds as the distribution of profit and debit the same directly to equity. However, if the issuer is or may be required to pay cash on these bonds, e.g., because the holder has a right to put these bonds to the issuer, these will be treated as liability and interest payable thereon will be treated as charge to profit or loss.

Recognition and measurement

Ind AS 109 requires balance sheet recognition for all financial instruments (including derivatives). It makes increased use of fair values than Indian GAAP. All financial assets and liabilities are initially recognized in the balance sheet at fair value. In the case of FVTPL assets, liabilities and derivatives (other than those used for hedging) and subsequent changes in fair value are recognized in profit or loss. The use of fair values is likely to cause volatility in the statement of profit and loss or other comprehensive income (OCI). To comply with Ind AS 109 requirement for fair value measurements, entities will have to make use of valuation methods and valuation professionals.

Impairment

Ind AS 109 requires a provision for impairment to be recognized based on the ECL model. To determine impairment loss, companies will need to consider information that is reasonably available at the reporting date about past events, current conditions and forecasts of future economic conditions. The need to incorporate forward-looking information means that application of Ind AS 109 will require considerable judgment as to how changes in macroeconomic factors will affect ECL.

Moreover, the focus on expected losses is likely to result in increased volatility in the amounts charged to profit or loss, especially for financial institutions (once Ind AS becomes applicable to them and from the group reporting perspective), while the increased level of judgment required in making the calculation may mean that it will be more difficult to compare the reported results of different entities. However, the more detailed disclosure requirements should provide greater transparency over an entity’s credit risk and provisioning processes.

Derecognition

Due to the application of Ind AS 109 derecognition requirements, an entity may not be able to derecognize financial assets transferred under the arrangements, such as, bill discounting and/or factoring of trade receivables, in entirety, if it has provided credit enhancement to the transferor. Rather, based on the specific facts, the entity will evaluate whether it should treat the transfer as a financing transaction (i.e., debt) or continuing involvement approach will apply which requires the entity to continue recognizing the transferred asset to the extent of its continuing involvement.

Comprehensive disclosures

Ind AS 107 requires very comprehensive disclosures regarding financial instruments and risks to which an entity is exposed, as well as the policies for managing such risks. Comprehensive information on the fair value of financial instruments would enhance the transparency and accountability of financial statements.
Business combinations

Key differences

- **Ind AS 103** *Business Combinations* applies to most business combinations, including amalgamations (where the acquiree loses its existence) and acquisitions (where the acquiree continues its existence).

  Under the current Indian GAAP, there is no comprehensive standard dealing with all business combinations. **AS 14 Accounting for Amalgamations** applies only to amalgamations, i.e., when acquiree loses its existence. **AS 10 Accounting for Fixed Assets** applies when a business is acquired on a lump-sum sale basis from another entity. **AS 21 Consolidated Financial Statements**, **AS 23 Accounting for Investments in Associates in Consolidated Financial Statements** and **AS 27 Financial Reporting of Interests in Joint Ventures** apply to accounting for investment in subsidiaries, associates and joint ventures, in the CFS respectively.

- **Ind AS 103** requires all business combinations within its scope, except business combinations under common control, to be accounted for under the acquisition method. Business combinations of entities or businesses under common control are accounted for using the pooling of interest method.

  Indian GAAP does not differentiate between common control and other business combinations. **AS 14** requires the pooling of interest method to be applied to an “amalgamation in the nature of merger,” which is an amalgamation that satisfies certain specified conditions. All the other amalgamations are accounted for using the purchase method.

- **Under Ind AS 103**, acquisition accounting is based on substance. Reverse acquisition is accounted for assuming the legal acquirer is the acquiree.

  Under Indian GAAP, acquisition accounting is based on legal form. Indian GAAP does not deal with reverse acquisitions.

- **Ind AS 103** requires net assets taken over, including contingent liabilities and intangible assets, to be recognized at fair value if certain specified criteria are met.

  Under Indian GAAP, when there is an acquisition of interest in subsidiaries, associates and joint ventures, the net assets are recognized at book value. Contingent liabilities of the acquiree are generally not recorded as liabilities under Indian GAAP. For amalgamation accounted for using the purchase method, **AS 14** allows accounting to be done on the basis of either the fair value or book value of the assets acquired and liabilities assumed.

- **Ind AS 103** prohibits amortization of goodwill arising on business combinations, and requires it to be tested for impairment annually.

  Under Indian GAAP, treatment of goodwill differs in different accounting standards. Goodwill arising from amalgamation in the nature of purchase is amortized to P&L over a period which may not exceed five years, unless somewhat longer period can be justified. Goodwill arising under **AS 10, AS 21, AS 23** and **AS 27** need not be amortized though there is no prohibition. After initial recognition, the acquirer measures goodwill at cost less accumulated amortization, if any, and accumulated impairment losses.

- **Ind AS 103** requires that contingent consideration in a business combination should be measured at fair value at the date of acquisition, and that this is included in the computation of goodwill/capital reserve arising on the business combination. Subsequent changes in the contingent consideration are not adjusted in goodwill, except for the measurement period adjustments. Subsequent accounting depends on whether the contingent consideration is equity, financial asset/financial liability. If it is classified as equity, it is not subsequently re-measured. If it is classified as financial asset or liability, subsequent changes are recognized in profit or loss.

  Under Indian GAAP, **AS 14** requires that where the scheme of amalgamation provides for an adjustment to consideration contingent on one or more future events, the amount of the additional payment is included in the consideration and consequently goodwill, if payment is probable and a reasonable estimate of the amount can be made. In all other cases, the adjustment is recognized as soon as the amount is determinable. No guidance is available for contingent consideration arising under other types of business combinations. This provides entities an option to use differing practices. The common practice is to adjust the goodwill.
Ind AS 103 specifically deals with accounting for pre-existing relationships between acquirer and acquiree, and for re-acquired rights by the acquirer in a business combination. It requires a reacquired right/pre-existing relationship to be recognized separately from the goodwill. An indemnification asset is initially measured on the same basis as the indemnified item, subject to the need for a valuation allowance for uncollectible items.

Indian GAAP does not provide guidance for such situations.

Ind AS 103 provides an option to measure any non-controlling (minority) interest in an acquiree at its fair value, or at the non-controlling interest's proportionate share of the acquiree's net identifiable assets. The choice of method is to be made for each business combination on a transaction-by-transaction basis, rather than being a policy choice.

Under Indian GAAP, AS 21 does not provide the first option to measure non-controlling (minority) interest in an acquiree at its fair value. It requires minority interest in a subsidiary to be measured at the proportionate share of book value of net assets.

Ind AS 103 requires that, in a business combination achieved in stages, the acquirer re-measures any previously-held equity interest in the acquiree at its acquisition date fair value. The acquirer is required to recognize the resulting gain or loss in profit or loss.

Under Indian GAAP, AS 21 recognizes step acquisitions. However, goodwill/capital reserve computation at each step is done on book values and historical cost basis, rather than fair values. Consequently, no gain/loss to be recognized in the statement of profit and loss can arise.

Key impact

The changes brought in by Ind AS 103 are likely to affect all stages of the acquisition process – from planning to the presentation of the post-deal results. The implications primarily involve providing increased transparency and insight into what has been acquired, and allowing the market to evaluate the management’s explanations of the rationale behind a transaction.

Reflection of true value of an acquisition

Following an acquisition, financial statements of the acquirer will look very different. Assets and liabilities will be recognized at fair value. Contingent liabilities and intangible assets that are not recognized in the acquiree’s balance sheet are likely to be recognized at fair value in the acquirer’s balance sheet. In a business combination achieved in stages, the acquirer will re-measure its previously-held equity interest in the acquiree at its acquisition date fair value. The acquirer will also have an option to measure non-controlling interest at fair value at the acquisition date. These changes in the recognition of net assets, and the measurement of previously-held equity interests and non-controlling interests, will significantly change the value of goodwill recorded in financial statements. Goodwill reflected in financial statements will project the actual premium paid by an entity for the acquisition.

Greater transparency

Significant new disclosures are required regarding the cost of the acquisition, the values of the main classes of assets and liabilities, and the justification for the amount allocated to goodwill. All stakeholders will be able to evaluate the actual worth of an acquisition and its impact on the future cash flow of the entity.

Significant impact on post-acquisition profits

Under Indian GAAP, net assets taken over are normally recognized at book value, and hence, charges to the statement of profit and account for amortization and depreciation expenses are based on carrying value. Under Ind AS, net assets taken over will be recognized at fair value. This will result in a charge to profit or loss for amortization and depreciation based on fair value, which is the true price paid by the acquirer for those assets. Goodwill is not amortized, but is required to be tested annually for impairment under Ind AS. Contingent considerations that are classified as financial liabilities are measured again through profit or loss in the subsequent period, rather than as an adjustment to goodwill. These items will increase volatility in the profit or loss.
Group accounts

Key differences

- Under Ind AS 110 Consolidated Financial Statements, each parent is required to present consolidated financial statements (CFS), in which it consolidates all its subsidiaries, subject to limited exemptions and exceptions. A parent need not present CFS if it meets all the following conditions:
  - It is a wholly-owned subsidiary or is a partially-owned subsidiary of another entity and all its other owners, including those not otherwise entitled to vote, have been informed about, and do not object to, the parent not presenting CFS
  - Its debt or equity instruments are not traded in a public market (a domestic or foreign stock exchange or an over-the-counter market, including local and regional markets)
  - It did not file, nor is it in the process of filing, its financial statements with a securities commission or other regulatory organization for the purpose of issuing any class of instruments in a public market, and
  - Its ultimate or any intermediate parent produces CFS that are available for public use and comply with Ind AS.

Under Indian GAAP, AS 21 does not mandate preparation of CFS. The Act requires that from accounting periods beginning or after 1 April 2014, all companies will prepare CFS. However, it contains the following exemptions:

- An intermediate wholly owned subsidiary is not required to prepare CFS, provided its holding company is located in India.
- On 16 January 2015, the MCA issued an amendment to the Companies Accounts Rules prescribing exemption for companies having one or more overseas subsidiaries. Though the amendment wordings are not clear, it appears that the amendment allows companies, having one or more foreign subsidiaries to prepare CFS as per any GAAP, instead of Indian GAAP. For example, a listed company having foreign subsidiaries is preparing IFRS CFS for submission to the stock exchange. The amendment will allow a company to use IFRS CFS for the Act purposes, instead of requiring them to prepare Indian GAAP CFS. This option is available only for one year, i.e., financial year beginning 1 April 2014 for a company having 31 March year-end.

- Companies having only associates and/or joint venture and no subsidiaries are required to prepare CFS from financial year beginning on or after 1 April 2015, instead of 1 April 2014.

Under Ind AS, a company will need to consider both Ind AS and the Act requirements to decide for preparation of CFS. Since there are differences in the requirements of two, the stricter of the two requirements is likely to apply.

- Under Ind AS 110, an investment entity that meets the specified definition is not required to present CFS. It is required to measure investments in all its subsidiaries, other than those that provide services relating to the investment entity’s investment activities, at fair value through profit or loss.

There is no such exception for investment entities under Indian GAAP.

- Ind AS 110 does not contain any exception for consolidation of subsidiaries other than exception related to investment entities.

AS 21 precludes consolidation of a subsidiary when either of the following conditions are met. In the CFS, such subsidiaries are accounted under AS 13 and the reasons for not consolidating are disclosed.

- Control is intended to be temporary because a subsidiary is acquired and held exclusively with a view to its subsequent disposal in the near future (generally, twelve months).
- A subsidiary operates under severe long-term restrictions, which significantly impair its ability to transfer funds to the parent.

- Ind AS 110 contains wide and substance-based definition of control. It identifies the principles of control, determines how to identify whether an investor controls an investee and therefore, must consolidate the investee. In accordance with Ind AS 110, an investor controls an investee if and only if the investor has all of the following elements:
Power over the investee, i.e., the investor has existing rights that give it the ability to direct the relevant activities (the activities that significantly affect the investee's returns). Such rights can either be straightforward (e.g., through voting rights) or be complex (e.g., embedded in contractual arrangements). An investor holding only protective rights cannot have power over an investee.

Exposure, or rights, to variable returns from its involvement with the investee. Such returns must have the potential to vary as a result of the investee's performance and can be positive, negative, or both.

Ability to use its power over the investee to affect the amount of the investor's returns. A parent must not only have power over an investee and exposure or rights to variable returns from its involvement with the investee, a parent must also have the ability to use its power over the investee to affect its returns from its involvement with the investee.

Under Indian GAAP, AS 21 defines control as ownership of majority voting rights and/or power to control the composition of the board of directors.

Under Ind AS 110, the existence of potential voting rights (e.g., options, convertible debentures) that are substantive are considered to assess whether an investor has power over an investee. Factors that are considered to assess whether potential voting rights are substantive include the exercise price, the financial ability of the investor to exercise and the exercise period.

AS 21 is silent on whether potential voting rights are to be considered for control. However, under AS 23, potential voting rights are not considered for determining significant influence in the case of an associate. Therefore, an analogy can be drawn that in the case of a subsidiary as well, potential voting rights are not to be considered for deciding control.

Ind AS 110 states an investor might have control over an investee even when it has less than a majority of the voting rights of that investee. The control exists if its rights are sufficient to give it power when the investor has the practical ability to direct the relevant activities of the investee unilaterally (a concept known as “de facto control”). When assessing whether an investor’s voting rights are sufficient to give it power, an investor considers all facts and circumstances, including:

- Size of the investor’s holding of voting rights relative to the size and dispersion of holdings of other vote holders
- Potential voting rights held by the investor, other vote holders or other parties
- Rights arising from other contractual arrangements, and
- Any additional facts and circumstances that indicate the investor has, or does not have, the current ability to direct relevant activities at the time that decisions need to be made, including voting patterns at previous shareholders’ meetings.

The concept of Defacto Control does not exist under Indian GAAP.

Ind AS 110 introduces a new concept of delegated power. An investor may delegate decision-making authority to an agent on some specific issues or on all relevant activities, but, ultimately, the investor, as principal, retains the power. An agent is a party engaged to act on behalf of another party (principal), but which does not have control over the investee. Accordingly, a decision maker that is not an agent is a principal. It is necessary to assess whether the decision maker is acting as a principal or an agent, to determine whether the decision maker is deemed to have control. Ind AS 110 provides guidance to analyze control, by asking whether the decision maker, is acting as a principal, or as an agent that is acting primarily on behalf of other investors.

The concept of Delegated Power does not exist under Indian GAAP.

Ind AS 110 introduces a new term “structured entities” (SE), which is an entity whose activities are restricted to the extent that they are not directed by a governing body. Ind AS 110 does not have “bright-line requirements” setting out when a reporting entity should consolidate an SE. Rather, an entity needs to consider all facts and circumstances to determine whether it has the power to direct the activities that cause the returns of the SE to vary.
The concept of SE does not exist under Indian GAAP.

Under Ind AS 110, compliance with uniform accounting policies is mandatory. If a member of the group uses accounting policies, other than those adopted in the CFS, for like transactions and events in comparable circumstances, appropriate adjustments are made to its financial statements in preparing the CFS to ensure conformity to the group's accounting policies.

Ind AS 28 provides an exemption from the requirement concerning uniform accounting policy on the grounds of impracticality only in case of associates (not for subsidiaries and joint ventures). Under Ind AS, applying a requirement is impracticable when the entity cannot apply it after making every reasonable effort to do so.

AS 21 requires that CFS should be prepared using uniform accounting policies for like transactions and other events in similar circumstances. If it is not practicable to use uniform accounting policies in preparing the CFS, that fact should be disclosed together with the proportions of the items in the CFS to which the different accounting policies have been applied. Indian GAAP provides an exemption on the grounds of impracticality for consolidation of subsidiaries, associates and joint ventures.

Under Ind AS, a maximum of three-month gap between the financial statements of a parent or investor and those of its subsidiary, associate or joint-ventures.

Indian GAAP allows a six-month gap for subsidiaries and jointly-controlled entities. For associates, there is no maximum time gap prescribed.

Under Ind AS, changes in ownership interests of a subsidiary (that do not result in the loss of control) are accounted for as an equity transaction, and have no impact on goodwill or the statement of profit and loss.

Indian GAAP does not provide any guidance on changes in ownership interest of a subsidiary that do not result in loss of control. This has resulted in existence of diverse practices on the matter.

Ind AS requires losses incurred by the subsidiary to be allocated between the controlling (parent) and non-controlling (minority) interests, even if it results in deficit balance of non-controlling interest.

Under Indian GAAP, excess losses attributable to minority shareholders over the carrying amount of minority interest are adjusted against the majority interest, unless the minority has a binding obligation to, and is able to, fund the losses.

Under Ind AS, in calculating gain/loss arising from the loss of control in CFS, retained interest in the former subsidiary is measured at its fair value at the date when control is lost.

AS 21 requires that in calculating gain/loss arising from the loss of control, retained interest in the former subsidiary is measured at proportionate amounts of its carrying value at the date when control is lost.

**Joint ventures**

Under Ind AS 111 Joint Arrangements, joint control is the contractually agreed sharing of control of an arrangement, which exists only when decisions about relevant activities, i.e., those that significantly affect the returns of the arrangement, require the unanimous consent of parties sharing control.

Under AS 27, joint control is the contractually agreed sharing of control over an economic activity. Control is the power to govern the financial and operating policies of an economic activity so as to obtain benefits from it.

Ind AS 111 classifies joint arrangements into:

- Joint operations whereby the parties that have joint control of the arrangement have rights to assets, and obligations for the liabilities, relating to the arrangement.
- Joint venture whereby the parties that have joint control of the arrangement have rights to the net assets of the arrangement.

AS 27 identifies three types of joint ventures — jointly controlled operations, jointly controlled assets and jointly controlled entities.

Under Ind AS 111, the structure of the arrangement is no longer the main factor in determining the accounting. An arrangement, which is structured through a separate vehicle, is not automatically classified as a joint venture. An assessment of the legal form of the separate vehicle, contractual terms and conditions and other facts and circumstances is still required before classifying an arrangement as a joint venture.

AS 27 uses only a legal entity or structure-based distinction between its joint-controlled entities and all other joint ventures. Accordingly, if an arrangement is structured in a separate legal entity, it is automatically classified as jointly controlled entity.
Under Ind AS 111, a joint venturer recognizes its interest in a joint venture as an investment and accounts for that investment using the equity method in accordance with Ind AS 28 Investments in Associates and Joint Ventures.

According to AS 27, in its consolidated financial statements, a venturer reports its interest in a jointly controlled entity using the proportionate consolidation.

Key impact

Changes in the group structure

Application of Ind AS 110 may significantly amend existing group structures as companies may need to consolidate additional subsidiaries based on criteria such as Defacto control, structured entities and potential voting rights. Moreover, some of the existing entities may get deconsolidated. Companies will need to update their existing group structures and start coordinating with new group entities so that they get timely information for all entities to prepare CFS.

Changes in group structure, as mentioned above, along with other Ind AS changes may significantly impact financial performance and financial position. It is necessary that entities start communicating such impacts to their stakeholders in advance to avoid sudden impact. Moreover, companies may need to renegotiate loan covenants based on their financial performance and financial position under Ind AS.

Exercise of significant judgment

Determination of control will become more judgmental. This is particularly relevant with regard to consideration of items as options and convertible instruments, structured entities and Defacto control. Since Ind AS 110 does not contain any bright line test on such determination, it is important that companies consider all the facts and circumstances in a comprehensive manner to arrive at an appropriate conclusion.

Continuous assessment

Ind AS 110 requires control to be assessed on a continuous basis. This is particularly relevant in marginal cases and may have “in, out and in” situation from one period to the next. For example, in case of Defacto control, a relatively small change in the shareholding pattern of an investee company may fail the control test. In subsequent periods, the entity may be able to achieve Defacto control again. This will result in significantly different numbers being used for consolidation.

Uniform accounting policies

The current Indian GAAP provides an exemption from the use of uniform accounting policies for the consolidation of subsidiaries, associates and joint ventures on the grounds of impracticality. Ind AS does not provide such an exemption, other than for associates, and mandates the use of uniform accounting policies for subsidiaries and joint ventures. This is likely to pose significant challenges. All entities will have to gear their systems, or develop systems such as preparation of group accounting manuals, to ensure compliance with this requirement. On conversion to Ind AS, many group entities will have to change their accounting policies to bring them in line with the parent entity.

Financial year-ends of all components in the group

The current Indian GAAP allows a maximum of six months gap between financial statements of a parent and a subsidiary, and that of a venturer and a joint venture. There is no maximum time limit prescribed for gap between financial statements of an investor and an associate. Ind AS allows a maximum of three months gap for subsidiaries, associates and joint ventures. On conversion to Ind AS, many companies may be compelled to change year-ends of their group entities to comply with this requirement and to avoid reporting results at multiple dates.

Service concession arrangements

Key differences

Under Indian GAAP, notified accounting standards do not deal with accounting for service concession arrangements (SCAs). In 2014, the ICAI has issued an exposure draft of the Guidance note on Accounting for Service Concession Arrangements by Concessionaires, which has not yet been finalized. In the absence of authoritative guidance, differing practices seem to have emerged to account for such arrangements and many companies seem to have followed differing practices. For instance, some companies have recognized “infrastructure asset” as a fixed asset, while others have recognized it as an intangible asset. Many companies do not recognize any revenue and profits during the construction period.
Appendix C Service Concession Arrangements of Ind AS 115 applies to public-to-private SCAs if they satisfy specified conditions. Applicability of Appendix C is restricted to public-to-private service concession arrangements (SCAs). Appendix C does not apply to all public-to-private SCAs. Rather, it prescribes the following criteria, all of which need to be met, for an arrangement to be within its scope:

▶ Grantor controls or regulates what services the operator must provide with the infrastructure, to whom it must provide them and at what price.

▶ Grantor controls, through ownership, beneficial entitlement or otherwise, any significant residual interest in infrastructure at the end of the arrangement period.

Appendix C of Ind AS 115 states that due to contractual service arrangement, the operator does not have a right to control the use of public service infrastructure covered within its scope. Rather, operator has access to operate the infrastructure for providing public service on behalf of grantor. Hence, operator should not recognize infrastructure covered within the scope of Appendix C as its property, plant and equipment (PPE). In substance, the operator acts as a service provider under the arrangement. It constructs/upgrades (construction service) the infrastructure used to provide public service, as well as operates and maintains (operation services) the same for a specified period. Hence, it will recognize and measure revenue arising from construction and operation services in accordance with Ind AS 115. The operator may receive (a) intangible assets (right to collect toll charges), (b) finance asset (right to receive annuity payments, for example, from the government authority), or (c) both against the services rendered. Hence, it will recognize consideration receivable as such in the financial statements. Under the intangible asset model, toll charges collected from users are recognized as revenue. Simultaneously, the company charges amortization of intangible asset to the statement of profit and loss. The financial asset model works similar to accounting for finance lease receivables, where amounts received are allocated between capital recovery and interest, using the effective interest method.

### Amortization of intangible assets

Ind AS 38 requires an intangible asset to be amortized over its expected useful life. In accordance with Ind AS 38, several methods may be used for amortization of an intangible asset with finite useful life. These methods include straight-line method, diminishing balance method and unit of production method. The methods used should be selected on the basis of expected pattern of consumption. For example, in a toll road concession, some argue that the number of vehicles using the road may be regarded as reflecting the pattern of consumption. Ind AS 38 prohibits the use of revenue-based amortization method. It states that an amortization method on revenue generated by an activity is inappropriate because it generally reflects factors other than the consumption of economic benefits of the asset. For example, revenue is affected by other inputs and processes, selling activities and changes in sales volumes and prices. The price component of revenue may be affected by inflation, which has no bearing upon the way in which an asset is consumed.

Under Indian GAAP, Schedule II to the Act allows companies to use revenue-based amortization for toll roads created under SCA. Considering this, certain companies amortize their toll roads using revenue-based amortization. Ind AS 101, read with Ind AS 38 scope paragraph, allows these companies an option to continue revenue-based amortization for toll roads recognized in the financial statements for period immediately before the beginning of the first Ind AS financial statements. It should be noted that this is an option. In other words, toll operators are free to use other basis that reflect the pattern of consumption, for example, the straight line method or amortization based on utilization of the road by vehicles. However, such amortization will not be allowed for any new toll road arising from SCA entered into after implementation of Ind AS.

### Key impact

#### Impact on revenue

Classification of the arrangement into intangible or financial asset under Ind AS will have a significant impact on the contract revenues recognized. For example, accounting under the intangible model would result in double the revenues compared to a contract with nearly identical cash flows that is accounted for using the financial asset model. Selection of the model to be applied is not an option. Rather, the model flows from whether the operator has the right to charge for services (intangible model) or the right to receive cash flows from the grantor (financial asset). This may require careful analysis, since a contract that initially appears to fall within the intangible model may have an element of guaranteed cash flows. For example, if during early years of the contract, the government body guarantees a minimum level of revenues from the operation of a new expressway to encourage private investment, there may be both a financial asset and an intangible asset.

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2 Please also refer the booklet titled “IFRS-converged Indian Accounting Standards - Outreach meeting dated 15 January 2015”, published by the Accounting Standards Board of the ICAI.
Estimates and fair values

Ind AS accounting for SCAs would involve an extensive use of estimates and valuations, which are expected to have a significant impact on the company’s financial statements. For example, construction revenues and costs need to be recognized for construction of the infrastructure. Since the contract is unlikely to specify separately the revenue from construction, it is necessary to allocate the contract revenues into various distinct individual performance obligations, i.e., construction, operations, maintenance, etc., based on their relative stand-alone selling prices. Companies may need to use either internal or external benchmarking for similar contracts, since an assessment of profitability on a SCA is normally made on an overall IRR basis and not separately for the construction and operation phases of the project.

Project finance implications

Two factors may impact the availability of project finance for contracts accounted under Appendix C. First, the PPE will be de-recognized from the balance sheet and replaced with either a financial or an intangible asset. Secondly, accounting for SCA will result in a mismatch between book profits and actual cash flows, particularly in case of a vanilla intangible asset model where profits on construction may be recognized several years in advance of the actual operating cash inflow. Financial institutions may need to be educated to focus attention on project cash flows instead of fixed assets and profits, so that companies are not disadvantaged on applying Appendix C. In the case of existing projects, companies will need to review loan covenants to assess whether the terms or covenants need to be adjusted in light of the different accounting model. A technical breach could occur, for example, if intangible or financial assets are not included in ratio tests applied in the loan covenant.

Income taxes

Key differences

- **AS 22 Accounting for Taxes on Income** is based on the income statement liability method, which focuses on timing differences. **Ind AS 12 Income Taxes** is based on the balance sheet liability method, which focuses on temporary differences. One example of temporary vs. timing difference approach is revaluation of fixed assets. Under Indian GAAP, no deferred tax is recognized on upward revaluation of fixed assets where such revaluation is credited directly to revaluation reserve. Under Ind AS, companies will recognize deferred tax on revaluation component if certain other recognition criteria are met.

- **Ind AS 12 requires the recognition of deferred taxes** in case of business combinations. Under Ind AS, the cost of a business combination is allocated to the identifiable assets acquired and liabilities assumed by reference to their fair values. However, if no equivalent adjustment is allowed for tax purposes, it would give rise to a temporary difference. Under Indian GAAP, business combinations (other than amalgamation) do not give rise to such deferred tax adjustment.

- **Ind AS 12** requires that when an entity has a history of tax losses, it recognizes deferred tax asset arising from unused tax losses or tax credits only to the extent that it has sufficient taxable temporary differences, or there is other convincing evidence that sufficient taxable profit will be available against which deferred tax asset can be realized. **Ind AS 12 does not lay down any requirement for consideration of virtual certainty** in such cases.

AS 22 under Indian GAAP requires that if the entity has carried forward tax losses or unabsorbed depreciation, all deferred tax assets are recognized only to the extent that there is virtual certainty supported by convincing evidence that sufficient future taxable income will be available against which such deferred tax assets can be realized.
Under Ind AS, an entity should recognize a deferred tax liability in CFS for all taxable temporary differences associated with investments in subsidiaries, branches and associates, and interests in joint ventures, except to the extent that the parent, investor or venturer is able to control timing of the reversal of temporary difference, and it is probable that the temporary difference will not reverse in the foreseeable future.

Under Indian GAAP, deferred tax is not recognized on such differences. Deferred taxes in the CFS are a simple aggregation of the deferred tax recognized by various group entities.

Under Ind AS, deferred taxes are recognized on temporary differences that arise from the elimination of profits and losses resulting from intra-group transactions.

Under Indian GAAP, deferred tax is not recognized on such eliminations. Deferred taxes in the CFS are a simple aggregation of the deferred tax recognized by various group entities.

Disclosure required for income taxes is likely to increase significantly on transition to Ind AS. Examples of certain critical disclosures mandated in Ind AS are: an explanation of the relationship between tax expense (income) and accounting profit; an explanation of changes in the applicable tax rate(s) compared to the previous accounting period; the amount (and expiry date, if any) of deductible temporary differences, unused tax losses, and unused tax credits for which no deferred tax asset is recognized in the balance sheet.

Under Indian GAAP, such disclosures are not required.

Key impact

Deferred tax accounting for the group

Under Indian GAAP, deferred taxes in the CFS are a simple aggregation of the deferred tax recognized by various group entities. On transition to Ind AS, deferred taxes in the CFS will be significantly different from that under Indian GAAP. This is because of GAAP differences explained above, especially with respect to undistributed profits of subsidiaries, associates and joint ventures and intra-group transactions.

Acquisitions

Deferred tax is recognized on fair value adjustment of acquired assets, liabilities and contingent liabilities recorded as part of business combination accounting. Goodwill under Ind AS is determined accordingly. Reversal of deferred tax asset/liability in future years affects the tax expense or income of those years. Therefore, the effect of acquisition on deferred taxes in future financial statements will differ significantly under Ind AS and Indian GAAP.

Entities in tax losses

Due to the strict principle of virtual certainty under Indian GAAP, only in very rare cases can entities recognize deferred tax assets where they have carried forward losses and unabsorbed depreciation. The “convincing evidence” principle under Ind AS is less stringent in comparison. Hence, the probability of recognizing deferred tax assets on carried forward tax losses and unabsorbed depreciation is higher under Ind AS. However, it will continue to require exercise of significant judgment.
Employee benefits and share-based payments

Key differences

- **Ind AS 19 Employee Benefits** requires the impact of remeasurement in net defined benefit liability (asset) to be recognized in other comprehensive income (OCI). Remeasurement of net defined benefit liability (asset) comprises actuarial gains or losses, return on plan assets (excluding interest on net asset/liability) and any change in effect of asset ceiling.

  AS 15 Employee Benefits under current Indian GAAP requires such actuarial gains and losses to be recognized in the statement of profit and loss.

- Under Ind AS 19, unvested past-service costs are recognized immediately as they occur, rather than being spread over the vesting period.

  AS 15 requires that an entity should recognize unvested past service cost as an expense on a straight-line basis over the average period until the benefits become vested.

- Under Ind AS, liability for termination benefits has to be recognized at the earlier of when the entity can no longer withdraw the offer of those benefits and when the entity recognizes a restructuring cost.

  Indian GAAP requires termination benefits liability to be recognized only when the entity has a present obligation as a result of a past event, it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation, and a reliable estimate can be made of the amount of the obligation.

- Ind AS 19 has significantly enhanced disclosure requirements for defined benefit plans. New disclosures mandated under Ind AS require information that explains the characteristics of its defined benefit plans and risks associated with them. These disclosures also reflect a sensitivity analysis for each significant actuarial assumption as of the end of the reporting period, showing how the defined benefit obligation would have been affected by changes in the relevant actuarial assumption that were reasonably possible at that date. The fair value of the plan assets should be disaggregated into classes that distinguish the nature and risks of those assets, subdividing each class of plan asset into those that have a quoted market price in an active market and those that do not.

- **Ind AS 102 Share-based Payment** applies to both employee and non-employee share-based payments.

  Under Indian GAAP, the Guidance Note on Accounting for Employee Share-based Payments, issued by the ICAI, covers only employee share based payments.

- Under Ind AS, employee share-based payments should be accounted for using the fair value method. Only in extremely rare circumstances, the entity is permitted to measure the equity instruments at their intrinsic value.

  Indian GAAP permits an option of using either the intrinsic value method or the fair value method. However, the entity using the intrinsic value method is required to give fair value disclosures.

- In case of graded vesting, Ind AS 102 requires an entity to determine the vesting period for each portion of the option separately, and amortize the compensation cost of each such portion on a straight-line basis over the vesting period of that portion. The option to recognize the expense over the service period for the entire award period is not available.

  Under Indian GAAP, the ICAI GN provides the following two options in this regard:

  - Determine the vesting period for each portion of the option separately, and amortize the compensation cost of each such portion on a straight-line basis over the vesting period of that portion.
  
  - The amount of employee compensation cost is accounted for and amortized on a straight-line basis over the aggregate vesting period of the entire option (that is, over the vesting period of the last separately vesting portion of the option). However, the amount of employee compensation cost recognized at any date should at least equal the fair value or the intrinsic value, as the case may be, of the vested portion of the option at that date.
Ind AS 102 deals with various issues arising from accounting for group and treasury share transactions. It requires the subsidiary, whose employees receive such compensation, to measure services received from its employees in accordance with Ind AS 102 with a corresponding increase recognized in equity as a contribution from the parent. Ind AS 102 also clarifies accounting for group cash-settled, share-based payment transactions in the separate (or individual) financial statements of an entity receiving the goods or services when another group entity or shareholder has the obligation to settle the award.

Under Indian GAAP, detailed guidance on issues arising from such transactions is not available. Common practice is that the entity whose employees receive such compensation does not account for any compensation cost because it does not have any settlement obligation.

**Key impact**

**Reduced volatility in profit or loss**

In the case of defined benefit plans, actuarial gains and losses arise due to changes in actuarial assumptions, such as with respect to discount rate, increase in salary, employee turnover, mortality rate, etc. The requirement to account for actuarial gains and losses in OCI will reduce volatility in the statement of profit and loss.

**Timing of recognition of termination benefits**

Under Ind AS, termination benefits are required to be provided when the scheme is announced and the management is demonstrably committed to it. Under Indian GAAP, termination benefits are required to be provided for based on legal liability (when employee signs up for the Voluntary Retirement Scheme (VRS) rather than constructive liability). Hence, there could be timing difference between creating a liability under Ind AS and Indian GAAP.

**True value of ESOP**

Indian GAAP permits entities to account for Employee Stock Ownership Plans (ESOPs), either through the fair value method or the intrinsic value method though disclosure is required to be made of the impact on profit or loss of applying the fair value method. It is observed that most Indian entities prefer to adopt the intrinsic value method. The drawback of this method is that it does not factor in option and time value when determining compensation cost. Under Ind AS, accounting for ESOPs will have to be remeasured using the fair value method. This may result in increased charges for ESOPs for many entities, and may have a significant impact on key indicators such as earnings per share.

**Accounting for share-based payments to non-employees**

It has been observed that many entities are entering into partnership agreements with their vendors to provide them with opportunities of sharing profits of a particular venture by offering them share-based payments. This mode of payment is considered as an incentive tool intended to encourage vendors to complete efficient and quality work. Under Indian GAAP, AS 10 requires a fixed asset acquired in exchange for shares to be recorded at its fair market value or the fair market value of the shares issued, whichever is more clearly evident. For other goods and services, there is no guidance on recognizing the cost of providing such benefits to vendors in lieu of goods or services received. Consequently, different accounting policies are being followed by Indian entities under current Indian GAAP. On transition to Ind AS, an entity will have to account for such benefits under the fair value method laid down in Ind AS 102.

**Accounting for group ESOPs**

In India, a subsidiary normally does not account for ESOPs issued to its employees by its parent entity, contending that clear-cut guidance is not available and it does not have any settlement obligation. Under Ind AS 102, such ESOPs will have to be accounted for according to principles laid down in Ind AS 102, i.e., either as equity-settled or as cash-settled plans, depending on specific criteria. In accordance with Ind AS 102, a receiving entity whose employees are being provided ESOP benefits by a parent will have to account for the charge. This will reflect true compensation cost of receiving employee benefits.
Property, plant and equipment, intangible assets, investment property, inventories and impairment

Key differences

Property, plant and equipment

- Ind AS 16 Property, Plant and Equipment mandates component accounting, whereas AS 10 Accounting for Fixed Assets recommends, but does not require it. However, the Act requires companies to apply component accounting mandatorily from the financial years commencing 1 April 2015.

- Major repairs and overhaul expenditure are capitalized under Ind AS 16 as replacement costs, if they satisfy the recognition criteria. In most cases, Indian GAAP requires these to be charged off to the statement of profit and loss as incurred.

- In accordance with Ind AS 16, cost of an item of PPE is its cash price equivalent at the recognition date. If the payment is deferred beyond normal credit terms, difference between the cash price equivalent and total payment is charged as interest expense to the statement of profit and loss over the credit period, unless such interest is capitalized under Ind AS 23 Borrowing Costs.

Except in the case of assets acquired on hire purchase, AS 10 does not require entities to separate finance element even if an asset is purchased on deferred payment basis. The general practice is not to discount the future cash flows.

- In accordance with Ind AS 16, the cost of an item of PPE includes initial estimate of the costs of dismantling and removing the item, and restoring the site on which it is located, the obligation for which an entity incurs either when the item is acquired or as a consequence of having used the item during a particular period for purposes other than to produce inventories during that period. In accordance with Ind AS 37 Provisions, Contingent Liabilities and Contingent Assets, the provision is created at the discounted amount.

Under Indian GAAP, AS 29 Provisions, Contingent Liabilities and Contingent Assets also requires upfront provision to be created for obligation to rectify the damage. However, such provision should be recognized at undiscounted amount. AS 10 or any other accounting standard does not provide any specific guidance on how the corresponding amount should be adjusted, except that the Guidance Note on Accounting for Oil and Gas Producing Activities states that entities involved in those activities should capitalize the dismantling and site restoration cost.

- Under Indian GAAP, paragraph 46A of AS 11 The Effects of Changes in Foreign Exchange Rates allows companies to adjust exchange differences arising on long-term foreign currency monetary item to the carrying value of PPE. However, such an option is not allowed under Ind AS 21 The Effects of Changes in Foreign Exchange Rates. Please refer discussion under the head “The effects of changes in foreign exchange rates” for further details.

- Schedule II to the Act, prescribes useful lives for various items of PPE. It also fixes residual value for items of PPE at 5% of the original cost. If a company adopts a useful life/residual value different from that specified in Schedule II, the financial statements should disclose such difference and provide justification in this behalf duly supported by technical advice. In accordance with the approach used in AS 6, a company has an option of treating the useful lives and residual value prescribed in Schedule II as maximum limit. Alternatively, the management can use the same as indicative only. The interaction of Schedule II and AS 6 is explained below:

  - The management has estimated the useful life of an asset to be 10 years. The life envisaged under the Schedule II is 12 years. In this case, AS 6 requires the company to depreciate the asset using 10 year life only. In addition, Schedule II requires disclosure of justification for using the lower life. The company cannot use 12 year life for depreciation.

  - The management has estimated the useful life of an asset to be 12 years. The life envisaged under the Schedule II is 10 years. In this case, the company has an option to depreciate the asset using either 10 year life prescribed in the Schedule II or the estimated useful life, i.e., 12 years. If the company depreciates the asset over the 12 years, it needs to disclose justification for using the higher life. The company should apply the option selected consistently.

Similar position will apply for the residual value.
Under Ind AS 16, an item of PPE is depreciated based on its estimated useful life and residual value. It is not acceptable to treat useful lives/residual value prescribed under Schedule II as maximum limit. However, if the management’s estimate of useful life and/or residual value is different vis-à-vis those prescribed in Schedule II, companies will need to disclose justification for using different useful life/residual value.

- Ind AS 16 requires estimates of useful lives, depreciation method and residual values to be reviewed at least at the end of each financial year. Indian GAAP does not mandate an annual review of these, but recommends periodic review of useful lives.

- Under Indian GAAP, any change in depreciation method is treated as an accounting policy change and applied retrospectively. Under Ind AS, it is treated as a change in accounting estimate and applied prospectively.

- Both Ind AS and Indian GAAP permit the revaluation model for subsequent measurement. If an asset is revalued, Ind AS 16 mandates revaluation to be done for the entire class of property, plant and equipment to which that asset belongs, and the revaluation to be updated periodically. Under Indian GAAP, revaluation is not required for all the assets of the given class. It is sufficient that the selection of the assets to be revalued is done systematically, e.g., an entity may revalue a class of assets of one unit and ignore the same class of assets at other location. Also, there is no need to update revaluation regularly under Indian GAAP.

### Intangible assets

- Under Ind AS 38 Intangible Assets, an intangible asset can have indefinite useful lives. Such assets are required to be tested for impairment at least on an annual basis and are not amortized.

Under Indian GAAP, AS 26 Intangible Assets does not recognize the concept of indefinite useful life of intangible assets. Rather, it contains a rebuttable presumption that useful life of an intangible asset should not exceed 10 years.

- Under Ind AS, an entity can choose revaluation model for subsequent measurement provided, there is an active market for the underlying intangible assets. Revaluation of intangible assets is prohibited under Indian GAAP.

- Ind AS 38 contains a rebuttable presumption that an amortization method based on the revenue generated by an activity that includes the use of an intangible asset is inappropriate and this presumption can be overcome only under limited circumstances.

AS 26 does not contain any such rebuttable presumption for amortization method based on revenue. Under Indian GAAP, Schedule II to the Act allows revenue-based amortization for toll roads created under the service concession arrangements (SCA). Considering this, certain Indian companies amortize their toll roads using revenue-based amortization. For further details on this matter, refer discussion under the head “Service concession arrangements.”

- Ind AS 38 requires an expenditure on advertising and promotional activities to be recognized as an expense when it is incurred. It further clarifies that an entity incurs this expenditure when it has an access to the underlying goods or when it receives the services. Therefore, it cannot defer the recognition of expenditure on advertising and promotional activities till these are delivered to customers.

AS 26 does not provide any such guidance. It is understood that under Indian GAAP, entities normally follow the practice of recognizing goods or services received for future advertising or promotional activities as an asset till these are delivered to the customers.

### Investment property

- Ind AS 40 Investment Property prescribes accounting and disclosure requirements for investment property in a detailed manner. Under Indian GAAP, AS 13 Accounting for Investment deals with investment property in a brief manner.

- Under Ind AS 40, investment property is measured using the cost model, i.e., at cost less accumulated depreciation and accumulated impairment, if any.

AS 13 requires investment property to be accounted for as long-term investment, i.e., at cost less other than temporary diminution in the value of property. Depreciation on investment property is required to be provided according to DCA Circular (10) CL-VI/61 dated 27 September 1961 and under AS 6. Hence, depreciated cost model is applied for subsequent measurement.

- Ind AS 40 requires all entities to disclose the fair value of its investment properties even though they are measured using the cost model.

Indian GAAP does not mandate fair value disclosures for investment property.
Inventories

- Ind AS 2 Inventories excludes from its scope only the measurement of inventories held by producers of minerals and mineral products, to the extent they are measured at net realizable value in accordance with well-established practices in those industries. It also states that any gains/losses arising from measuring inventories at net realizable value are recognized in profit or loss in the period of change.

- AS 2 Valuation of Inventories excludes from its scope all aspects of accounting for producers' inventories of mineral oils, ores and gases, to the extent that they are measured at net realizable value in accordance with well-established practices in those industries.

- Ind AS 2 acknowledges that a broker-trader may decide to measure its inventories at fair value less cost to sell. If this is the case, Ind AS 2 does not apply to measurement of inventories and broker-traders recognize gain/loss arising from measurement at fair value less cost to sell in profit or loss for the period.

- AS 2 applies to commodity broker-traders. Hence, they need to measure inventories at lower of cost and net realizable value under current Indian GAAP.

- Ind AS 2 requires that where inventory is acquired on deferred settlement terms, the entity should identify finance element separately. The difference between the cash price equivalent and the total payment is recognized as an interest over the period of financing.

- Both under Ind AS 2 and AS 2, specific identification, FIFO and weighted average cost methods are acceptable methods of determining cost. However, their criterion for the use of methods is different. Ind AS 2 requires that the same cost formula should be used consistently for all inventories that have a similar nature and use to the entity. AS 2 requires that the formula used should reflect the fairest possible approximation to the cost incurred in bringing the items of inventory to their present location and condition.

Impairment of assets

- Ind AS 36 Impairment of Assets is applicable to investments in subsidiaries, associates and joint ventures in the separate financial statements of the parent. In accordance with Ind AS 28, interests in joint ventures and associates included in the CFS by way of the equity method are also within the scope of Ind AS 36.

- AS 28 Impairment of Assets does not apply to impairment of the above assets.

- Ind AS 36 requires that an entity should estimate the following assets for impairment at least annually even if there is no indicator of impairment. This impairment test may be performed at any time during an annual period, provided it is performed at the same time every year.
  - An intangible asset with an indefinite useful life
  - An intangible asset that is not yet available for use
  - Goodwill acquired in a business combination

Under Indian GAAP, an entity needs to test the following assets for impairment at least at each financial year end even if there is no indication that the asset is impaired. AS 28 does not require annual impairment testing for the goodwill unless there is an indication of impairment.

- An intangible asset that is not yet available for use
- An intangible asset that is amortized over a period exceeding 10 years from the date when the asset is available for use.

- Under Ind AS 36, goodwill is allocated to cash generating units (CGUs) or groups of CGUs that are expected to benefit from the synergies of the business combination from which it arose. There is no bottom-up or top-down approach for allocation of goodwill.

Under AS 28, goodwill is allocated to CGUs only when the allocation can be done on a reasonable and consistent basis. If that requirement is not met for a specific CGU under review, the smallest CGU to which the carrying amount of goodwill can be allocated on a reasonable and consistent basis must be identified and the impairment test carried out at this level. Therefore, when all or a portion of goodwill cannot be allocated reasonably and consistently to the CGU being tested for impairment, two levels of impairment tests are carried out, i.e., bottom-up test and top-down test.

- Ind AS 36 does not permit an impairment loss recognized for goodwill to be reversed in a subsequent period.
AS 28 requires that impairment loss recognized for goodwill should be reversed in a subsequent period when it was caused by a specific external event of an exceptional nature that is not expected to recur and subsequent external events have occurred that reverse the effect of that event.

Ind AS 36 requires additional disclosures for one CGU or group of CGUs, if the carrying amount of goodwill or intangible assets with indefinite useful lives allocated to the CGU or group of CGUs is significant in comparison with the entity’s total goodwill or intangible assets with indefinite lives. The disclosure required primarily deal with the key assumptions used to measure the recoverable amounts of such CGU or groups of CGUs. Disclosures required also include headroom and impact of reasonably possible changes in key assumptions.

AS 28 does not require any such disclosure.

Key impact

Component accounting

Under Ind AS 16, a component of an item of PPE with a cost that is significant in relation to total cost of the item will be separately depreciated. Hence, entities will need to divide the cost of an asset into significant parts, if their useful life is different, and depreciate them separately. This will require entities to restructure their fixed asset register and recompute depreciation. Furthermore, the requirement of estimating residual value is likely to change depreciation of many assets, as Indian companies normally presume 5% of the value of assets as their residual value, rather than making any estimate of the residual value. It may be noted that component accounting is a requirement under the Act also from financial years beginning on or after 1 April 2015, and even companies that continue to follow Indian GAAP will have to carry out component accounting.

Revaluation of fixed assets

Indian entities, which have selectively revalued fixed assets or intend to revalue the fixed assets, will have to determine whether they want to continue with the revaluation model or not. This decision is crucial for an entity if it wants to continue with the revaluation model. It will have to:

- Adopt the revaluation model for the entire class of assets that cannot be restricted to some selective location
- Update such revaluation on regular basis
- Take a depreciation charge in the statement of profit and loss based on revalued amounts to be updated regularly.

Intangible assets

Unlike Indian GAAP, amortization will not be required under Ind AS for an intangible asset for which there is no foreseeable limit on the period over which the asset is expected to generate net cash inflow for the entity. However, annual impairment testing will be required for such an asset. This can create volatility in profit or loss. Moreover, the company will be able to reflect intangible assets at their fair value, provided there is an active market for them. This will help the company project real value of their intangible assets in the balance sheet to their stakeholders.
Provisions, Contingent Liabilities and Contingent Assets

Key differences

Ind AS 37 Provisions, Contingent Liabilities and Contingent Assets does not apply to all financial instruments (including financial guarantees) that are within the scope of Ind AS 109 Financial Instruments.

AS 29 Provisions, Contingent Liabilities and Contingent Assets excludes from its scope only those financial instruments, which are carried at fair value. Therefore, it applies to financial instruments (including financial guarantees) that are not carried at fair value.

Ind AS 37 specifically requires provision to be created for constructive obligations if other criteria for recognition of provision are also met. A constructive obligation is an obligation that derives from an entity's actions where:

- By an established pattern of past practice, published policies or a sufficiently specific current statement, the entity has indicated to other parties that it will accept certain responsibilities, and
- As a result, the entity has created a valid expectation on the part of those other parties that it will discharge those responsibilities.

AS 29 does not specifically recognize the concept of constructive obligations. However, it requires creation of provisions arising out of normal business practices, custom and a desire to maintain good business relations or to act in an equitable manner.

Ind AS 37 requires that where the effect of time value of money is material, the amount of provision should be the present value of the expenditures expected to be required to settle the obligation. Ind AS 37 also provides that where discounting is used, the carrying amount of a provision increases in each period to reflect the passage of time. This increase is recognized as borrowing cost.

AS 29 prohibits discounting the amounts of provisions.

Under Ind AS 37, restructuring provision is made based on constructive obligation. In contrast, AS 29 requires restructuring provision to be made based on legal obligation.

Ind AS 37 requires disclosure of contingent assets in the financial statements when the inflow of economic benefits is probable. The disclosure, however, should avoid misleading indications of the likelihood of income arising.

AS 29 prohibits disclosure of contingent asset in the financial statements. However, it can be disclosed in the Director's Report, where inflow of economic benefits is probable.

Leases

Key differences

Ind AS 17 Leases deals with lease of land and composite leases. It requires a lease of land to be assessed as an operating or finance lease, based on the same criteria that are applicable for lease of other assets. Ind AS 17 also states that when a lease includes both land and building elements, an entity assesses the classification of each element as finance or an operating lease separately in accordance with the criteria laid in the standard. In determining whether the land element is an operating or a finance lease, an important consideration is that land normally has an indefinite economic life.

AS 19 excludes lease of land from its scope. Consequent to this, disparate practices have emerged with regard to accounting for short-term and long-term leases of land as well as composite leases of land and building. An opinion issued by the EAC provides guidance on long-term lease of land. In accordance with the opinion, a lease of land for very long period has the effect of passing significant rights of ownership. Therefore, such a lease will be in the nature of sale and should be accounted for accordingly.
Under Ind AS 17, lease rentals under an operating lease are recognized as an expense/income on a straight-line basis over the lease term unless:

- Another systematic basis is more representative of the time pattern of the user’s benefit even if the payments to the lessors are not on that basis.
- Lease rentals are structured to increase in line with expected general inflation to compensate for the lessor’s expected inflationary cost increases. If payments to the lessor vary because of factors other than general inflation, then this condition is not met.

Hence, Ind AS 17 does not mandate straight-lining of lease escalation if they are in line with the expected general inflation compensating the lessor for expected inflationary cost.

Under AS 19, lease rentals under an operating lease are recognized as an expense/income on a straight-line basis over the lease term unless another systematic basis is more representative of the time pattern of the user’s benefit even if the payments to the lessors are not on that basis. This view is further reiterated in certain EAC opinions.

If a sale and leaseback transaction results in a finance lease, Ind AS 17 requires that any excess of sale proceeds over the carrying amount is not immediately recognized as income by a seller-lessee. Instead, it is deferred and amortized over the lease term. However, it does not prescribe any particular method of amortization.

AS 19 requires both excess and deficiency to be deferred and amortized. AS 19 requires such excess/deficiency to be amortized over the lease term in proportion to the depreciation on the leased asset.

The application of Ind AS will require entities to carefully examine the terms of an arrangement to determine whether it is, or contains, a lease. Appendix C to Ind AS 17 provides the following two criteria, which if met, will indicate the existence of a lease:

a) Fulfilment of the arrangement is dependent on the use of a specific asset or assets (the asset), and
b) The arrangement conveys a right to use the asset

These two criteria are not straightforward and require a careful analysis in each case.

**Dependence on the use of a specific asset**

An arrangement may contain a lease when the contract explicitly requires a specific asset to be used. The arrangement may also contain a lease when no asset is specified but it is not economically feasible or practicable for the supplier to use an alternative asset, for example when the asset has been developed specifically to meet the purchaser’s needs or when the supplier owns only one suitable asset. On the other hand, when a specific asset is explicitly identified by the arrangement, but the seller has the right and the ability to provide the relevant goods using other assets not specified in the agreement, the arrangement will not contain a lease.

**Conveys a right to use the asset**

Once a specific asset is identified, there must then be an assessment as to whether there is a right of use, which is essentially a right to control the use of the underlying asset. Appendix C to Ind AS 17 refers to three conditions that can indicate such a right of use exists, of which only one needs to be met. These three conditions are:

a) The purchaser has the ability or right to operate the asset or direct others to operate the asset in a manner it determines while obtaining or controlling more than an insignificant amount of the output or other utility of the asset.
b) The purchaser has the ability or right to control physical access to the underlying asset while obtaining or controlling more than an insignificant amount of the output or other utility of the asset.

**Determining whether an arrangement contains a lease**

Many companies enter into arrangements for sale, purchase or other service arrangements that do not take the legal form of lease; but nevertheless they convey a right to use an asset such as an item of property, plant or equipment for an agreed period of time in return for a payment or series of payments. AS 17 under current Indian GAAP does not contain any specific guidance requiring identification of leases contained in a transaction structured as sale, purchase or rendering of service. In the absence of such guidance, entities typically do not identify leases contained in such arrangements; rather, such transactions are generally accounted based on their legal form.
c) Facts and circumstances indicate that it is remote that one or more parties other than the purchaser will take more than an insignificant amount of the output or other utility that will be produced or generated by the asset during the term of the arrangement. Furthermore, the price that the purchaser will pay for the output is neither contractually fixed per unit of output nor equal to the current market price per unit of output as of the time of delivery of the output.

Key impact

Service contracts

Under Ind AS, an embedded lease may exist in sale/purchase/service contracts entered by entities in any industry. Given below are some contracts that are most susceptible to a lease classification:

- Outsourcing arrangements, e.g., the outsourcing of an entity’s data processing, storage or other functions such as manufacturing
- Exclusive sale/purchase/supply contracts
- Suppliers of network capacity that provide purchasers with rights to capacity, e.g., in the telecommunications industry
- Power purchase agreement or other take-or-pay contracts requiring the purchaser to make specified payments regardless of whether it takes delivery of the contracted products or services
- Transportation contracts involving the provision of specific vehicles

If an entity determines that an arrangement is, or contains, a lease, the subsequent accounting for the lease element will be covered under Ind AS 17. For example, an entity determines whether a lease is an operating lease or a finance lease based on Ind AS 17 criteria.

If leases are identified as finance lease, the entity will derecognize the asset completely and recognize lease payments receivable. The asset and finance lease liability is recognized by the customer.

Apart from the impact on financial statements, such accounting may also have significant business implications for both the lessor and lessee, for example, compliance with debt covenants, measurement of EBITDA, presentation of revenue and cost numbers and ability to raise further finance.

The effects of changes in foreign exchange rates

Key differences

- Ind AS 21 The Effects of Changes in Foreign Exchange Rates is based on the concept of functional currency. It defines the ‘functional currency’ as the currency of the primary economic environment in which an entity operates. It lays down specific criteria to determine the functional currency of an entity. In accordance with Ind AS 21, each individual entity determines its functional currency and measures its results, and financial position in that currency. Based on prescribed criteria, it is possible that certain Indian entities may identify currencies other than INR as their functional currency.

- AS 11 The Effects of Changes in Foreign Exchange Rates is based on the concept of ‘reporting currency.’ It defines the term ‘reporting currency’ as ‘the currency used in presenting the financial statements.’ AS 11 does not specify the currency in which an entity should present its financial statements. However, an entity normally uses the currency of the country in which it is domiciled. If an entity uses a different currency, it needs to disclose the reason for using that currency. Considering the requirements of the Companies Act, 1956 (including its Schedule VI) and the Companies Act, 2013 (including its Schedule III), Indian companies typically use INR as their reporting currency.

- Ind AS 21 does not make distinction between integral and non-integral foreign operations. All entities are required to prepare their financial statements in their functional currency. Any exchange gain/loss to recognize a transaction in its functional currency is recognized in the profit or loss for the period. In translating the financial statements from functional currency to presentation currency, a reporting entity should use the following procedures:
  - Assets and liabilities, both monetary and non-monetary, should be translated at the closing rate.
  - Income and expense items should be translated at exchange rates at the dates of the transactions.
  - All resulting exchange differences should be recognized in OCI and accumulated in the foreign currency translation reserve, until the disposal of the net investment.
AS 11 distinguishes between integral and non-integral foreign operations and accordingly prescribes separate accounting treatment for integral and non-integral operations. The financial statements of an integral foreign operation should be translated using the principles and procedures as if the transactions of the foreign operation had been those of the reporting entity itself. In translating the financial statements of a non-integral foreign operation, the reporting entity follows translation procedures which are similar to translation into presentation currency under Ind AS 21.

AS 11 gives two options with regard to accounting for exchange differences. The first option is that an entity recognizes exchange differences as income or expense in profit or loss for the period in which they arise. However, AS 11 also provides companies an option to adopt the following accounting treatment for exchange differences arising on long-term foreign currency monetary items. The option once selected is irrevocable and needs to be applied to all long-term foreign currency monetary items. A long-term foreign currency monetary item is an item having a term of 12 months or more at the date of its origination.

- If the long-term foreign currency monetary item relates to acquisition of a depreciable capital asset, exchange differences arising on such monetary items are added to or deducted from the cost of the asset and are depreciated over the remaining useful life of the asset.

- If the long-term foreign currency monetary item relates to other than acquisition of a depreciable capital asset, exchange differences are accumulated in the “Foreign Currency Monetary Item Translation Difference Account” and amortized over the life of such long-term asset or liability.

- Exchange differences arising on short-term foreign currency monetary items are recognized immediately as income or expense in profit or loss for the period.

However, Ind AS 21 contains scope exclusion for companies which have applied the second alternative to defer/capitalize exchange differences under AS 11. In accordance with the exclusion, these companies have an option to continue applying their Indian GAAP policy for accounting of exchange differences arising on translation of long-term foreign currency monetary items recognized in the financial statements for the period ending immediately before the beginning of the first Ind AS financial reporting period. However, this option is not allowed for any new long-term foreign currency monetary item recognized after the implementation of Ind AS. This aspect is further elaborated under the head ‘First-time adoption of Ind AS’.

Key impact

Compliance with local laws

Ind AS recommends that the local statutory and tax requirements should not be considered when determining the functional currency. If an Indian company concludes that INR is not its functional currency, it may need to use a dual currency ledger to capture financial information in both the local currency and the functional currency to comply with both local tax and other laws, as well as Ind AS requirements.

First-time adoption

Ind AS 101 does not contain an exemption allowing a first-time adopter to use a currency other than the functional currency in determining the cost of assets and liabilities. Consequently, a first-time adopter that measured transactions in a currency that is not its functional currency will need to restate its financial statements with retrospective effect. For a large entity with numerous assets, this may be an onerous exercise as it will affect the measurement of all non-monetary items in the opening Ind AS balance sheet.
Presentation of financial statements

Key differences

- **Ind AS 1 Presentation of Financial Statements** is significantly different from the corresponding AS 1 Disclosure of Accounting Policies. While Ind AS sets out overall requirements for the presentation of financial statements, guidelines for their structure and minimum requirements for their content, AS 1 deals only with disclosure of accounting policies. It does not prescribe any overall requirements for presentation of financial statements. The format and disclosure requirements are set out under Schedule III to the Companies Act, 2013.

  The Ministry of Corporate Affairs (MCA) has still not prescribed Ind AS compliant Schedule III. The ICAI had issued an exposure draft of the Ind-AS compliant Schedule III for companies other than NBFCs, for public comments. However, it is still not final.

- Ind AS introduces the concept of comprehensive income, which requires all changes in equity (other than those attributable to transactions with owners) to be presented as part of the statement of profit and loss as a separate component titled “Other comprehensive income”.

  Under Indian GAAP, there is no concept of comprehensive income. AS 5 requires all items of income and expenses to be recognized in the statement of profit and loss, unless required otherwise by any other accounting standard.

- Ind AS 1 requires presentation of all transactions with equity holders in their capacity as equity-holders in the statement of changes in equity (SOCIE). The SOCIE is considered to be an integral part of financial statements.

  The concept of a SOCIE is not present under Indian GAAP; however, information relating to appropriation of profits, movement in capital and reserves, etc., is presented in the notes to financial statements.

- Among other disclosures, Ind AS 1 requires disclosure of:
  - Critical judgments made by management in applying accounting policies
  - Key sources of estimation uncertainty that have a significant risk of causing a material adjustment to the carrying amounts of assets and liabilities within the next financial year
  - Information that enables users of its financial statements to evaluate the entity’s objectives, policies and processes for managing capital

  There are no such disclosures required under current Indian GAAP.

- Ind AS 1 prohibits any item to be presented as an extraordinary item, either on the face of the income statement or in the notes.

  AS 5 Net Profit or Loss for the Period, Prior Period Items and Changes in Accounting Policies, in Indian GAAP, specifically requires disclosure of certain items as extraordinary items.

- Ind AS 1 requires a third balance sheet as at the beginning of the earliest comparative period, where an entity applies an accounting policy retrospectively or makes a retrospective restatement of items in its financial statements, or when it reclassifies items in its financial statements, to be included in a complete set of financial statements.

  AS 5 requires the impact of material changes in accounting policies to be shown in financial statements for current period. There is no requirement to present an additional balance sheet.

- Under Ind AS 1, an entity whose financial statements comply with Ind AS is required to make an explicit and unreserved statement of such compliance in the notes.

  Such requirement is not there in current Indian GAAP.

- Ind AS 1 acknowledges that in rare circumstances, compliance with a requirement in an Ind AS may be so misleading that it will conflict with the objective of financial statements set out in the Framework. In such cases, the entity should depart from that requirement if the relevant regulatory framework requires, or otherwise does not prohibit, such a departure. Ind AS 1 also prescribes detailed disclosures to explain departure and its impact.

  The current Indian GAAP does not recognize true and fair override, and compliance with all notified accounting standards is mandatory.
Ind AS 8 Accounting Policies, Changes in Accounting Estimates and Errors recognizes that there will be circumstances where a particular event, transaction or other condition is not specifically addressed by Ind AS. When this is the case, Ind AS 8 sets out a hierarchy of guidance to be considered in the selection of an accounting policy. The primary requirement is that management should use its judgment in developing and applying an accounting policy that results in information that is (i) relevant to the economic decision-making needs of users, and (ii) reliable.

Indian GAAP does not contain any specific guidance on how an entity will select accounting policy if a particular event, transaction or other condition is not specifically addressed by an accounting standard.

Ind AS 8 requires that when an entity changes an accounting policy voluntarily, then it will apply the change retrospectively. In other words, the entity will apply revised accounting policy to transactions, other events and conditions as if the revised policy had always been applied. The standard requires the entity to adjust the opening balance of each affected component of equity for the earliest prior period presented and the other comparative amounts disclosed for each prior period presented.

AS 5 under Indian GAAP does not provide any specific guidance on whether the change needs to be applied prospectively or retrospectively and how its impact should be dealt with, except that AS 6 Depreciation Accounting requires change in method of depreciation to be applied retrospectively. In the absence of specific guidance, differing practices are being followed with regard to application of voluntary change in accounting policy.

Ind AS 8 requires that when an entity has not applied a new Ind AS, which has been issued but is not yet effective, the entity should disclose:

- This fact, and
- Known or reasonably estimable information relevant to assessing the possible impact that application of the new Ind AS will have on the entity’s financial statements in the period of initial application.

Indian GAAP does not contain this requirement.

Ind AS 8 treats all omissions/misstatements in an entity’s earlier period financial statements, including balance sheet misclassifications, as an error/prior period item.

Under AS 5, a prior period item includes only the items of income and expense arising in the current period from errors or omissions in the earlier period financial statements. Therefore, balance sheet misclassifications not impacting the statement of profit and loss are not treated as “prior period item” under AS 5.

Ind AS 8 requires that an entity will correct prior period errors retrospectively in the first set of financial statements approved for issue after their discovery by restating the comparative amounts for the prior period(s) presented in which the error occurred. If the error occurred before the earliest prior period presented, it will restate the opening balances of assets, liabilities and equity for the earliest prior period presented. Ind AS 8 does not require restatement of prior periods only if such a restatement is impracticable.

AS 5 requires the impact of prior period items to be included in the current year statement of profit and loss, with a separate disclosure. Comparative information of earlier years is not restated.

Ind AS 8 provides considerable guidance to explain what “impracticable” means. Applying a requirement is impracticable when an entity cannot apply it after making every reasonable effort to do so.

The current Indian GAAP does not define the term “impractical”.

Ind AS includes numerous additional presentation and disclosure requirements vis-à-vis those required under Indian GAAP. Nearly each Ind AS contain additional disclosures as compared to those required under Indian GAAP. For example, Ind AS 113 Fair Value Measurement requires comprehensive disclosures for assets and liabilities which are measured at fair value and also for items which are not measured at fair value but otherwise require fair value disclosures.

Ind AS 107 Financial Instruments: Disclosures requires extensive disclosures about the risks arising from financial instruments and how they are managed. To comply with these requirements, both qualitative and quantitative disclosures are required.

Ind AS 103 requires extensive disclosures for business combinations.

Similar disclosures are not required under Indian GAAP.
Key impacts

Consistency with the Companies Act

In the case of voluntary change in accounting policy, Ind AS 8 requires that comparative amount appearing in the current period financial statements should be restated. A similar requirement also applies for correction of an error and recategorisation of previous period amounts. One may argue that these requirements are not in sync with section 131(1) of the Act dealing with voluntary revision of financial statements. In accordance with the section, the directors of a company may prepare revised financial statements only after obtaining approval of the Tribunal.

Once Ind AS becomes applicable, an issue will arise whether restatement of comparative amounts appearing in the current period financial statements tantamounts to revision of financial statements. If so, the companies will need to obtain the Tribunal approval for applying each change in policy, recategorisation and correction of error. This will be a very time-consuming exercise. To address this aspect, the MCA may clarify that if a company restates comparative amount appearing in the current period financial statements to comply Ind AS, this will not be treated as re-opening/revision of previous year financial statements under section 131(1).

Enhanced transparency and accountability

Disclosures required by Ind AS will significantly increase transparency and accountability of the financial statements. For example, Ind AS 1 requires disclosure of critical judgments made by management in applying accounting policies and key sources of estimation uncertainty that have a significant risk of causing a material adjustment to the carrying amounts of assets and liabilities within the next financial year. This is likely to not only bring improved transparency in financial statements, but it is also expected to put additional onus on entities to ensure that estimates and judgments made are justifiable, since, they are publicly accountable for them.

Identification and fulfilment of data gaps

The application of Ind AS will give rise to significant additional disclosures in the financial statements. The reviews of the 2005 financial statements of European companies suggested that financial disclosures under IFRS increased by more than 30%, as compared with their previous disclosures. To comply with additional disclosure requirements, management should identify “data gaps” early on so that any information that needs to be captured can be captured and recorded for all periods required to be converted.

Related party disclosures

Key differences

- Definition of “related party” under Ind AS 24 is broader and will cover increased number of related party relationship than AS 18. Ind AS 24 uses the following broad approach to identify related parties:
  - When an entity assesses whether two parties are related, it would treat significant influence as equivalent to the relationship that exists between an entity and a member of its key management personnel. However, those relationships are not as close as a relationship of control or joint control.
  - If two entities are both subject to control (or joint control) by the same entity or person, the two entities are related to each other.
  - If one entity (or person) controls (or jointly controls) a second entity and the first entity (or person) has significant influence over a third entity, the second and third entities are related to each other.
  - Conversely, if two entities are both subject to significant influence by the same entity (or person), the two entities are not related to each other.
  - If, based on Ind AS 24 definition, one party is identified as related to the second party; the definition would treat the second party as related to the first party, by symmetry.

There are no such clear principles for identification of related parties under AS 18. Particularly, AS 18 definition is not based on the principle of reciprocity.

- Ind AS 24 includes close members of families of key management personnel (KMP) as related party as well as that of persons who exercise control/significant influence over the entity.

- AS 18 includes only relatives of KMPs as related party.

- Under Ind AS 24, definition of KMP includes any director whether executive or otherwise. AS 18 excludes non-executive directors from the definition of KMP.

- According to Ind AS 24, an entity discloses that terms of related party transactions are equivalent to those that prevail in arm's length transactions, only if such terms can be substantiated.
AS 18 has no such stipulation on substantiation of related party transactions when the same is disclosed to be on arm’s length basis.

- Ind AS 24 requires disclosure of key management personnel’s compensation in total and for specified categories, such as short-term employee benefits and post-employment benefits.

AS 18 does not have such requirement.

- Ind AS 24 defines the term “government-related entity” as “an entity that is controlled, jointly controlled or significantly influenced by a government”. Ind AS 24 exempts a reporting entity from making disclosures pertaining to related party transactions and outstanding balances, including commitments, with:

  - A government that has control or joint control of, or significant influence over, the reporting entity, and

  - Another entity that is a related party because the same government has control or joint control of, or significant influence over, both the reporting entity and the other entity

If a reporting entity applies the above exemption, it should still make certain specified disclosures about transactions and related outstanding balances.

In accordance with AS 18, a state-controlled entity is an entity, which is under the control of the Central Government and/or any state government(s). AS 18 does not require disclosure in the financial statements of state-controlled entities as regards to related party relationships with other state-controlled entities and transactions with such entities.

Key impact

Entities will be required to reassess the list of related parties for enhanced relationships, which is covered under the scope of definition of related party in Ind AS 24.

It is noted that in the revised Clause 49, definition of the term “related party” includes related parties according to applicable accounting standards. Hence, on the application of Ind AS, the approval requirements under the SEBI Clause 49 for related party transactions will also get triggered for transactions with related parties within the scope of Ind AS 24.

Entities will need to strengthen/change their reporting processes and information technology systems to map new related parties covered in Ind AS 24 and track transactions with specific related parties.

### Segment reporting

#### Key differences

- Ind AS 108 Operating Segments adopts management reporting approach to identify operating segments. It is likely that in many cases, the structure of operating segments will be the same under Ind AS 108 as under AS 17 Segment Reporting. This is because AS 17, like Ind AS 108, considers reporting segments as the organizational units for which information is reported to key management personnel for the purpose of performance assessment and future resource allocation. When an entity’s internal structure and management reporting system is based on either product lines or geography, AS 17 requires the entity to choose one as its primary segment reporting format. Ind AS 108, however, does not impose this requirement to report segment information on a product or geographical basis and in some cases this may result in different segments being reported under Ind AS 108 as compared with AS 17.

- An entity is first required to identify all operating segments that meet the definition in Ind AS 108. Once all operating segments have been identified, the entity must determine which of these operating segments are reportable. If a segment is reportable, then, it must be separately disclosed. This approach is the same as that required by AS 17, except that it does not require the entity to determine a “primary” and “secondary” basis of segment reporting.

- Ind AS 108 requires that the amount of each segment item reported is the measure reported to the Chief Operating Decision Maker (CODM) in internal management reports, even if this information is not prepared in accordance with the Ind AS accounting policies of the entity. This may result in differences between the amounts reported in segment information and those reported in the entity’s primary financial statements. In contrast, AS 17 requires segment information to be prepared in conformity with the entity’s accounting policies for preparing its financial statements.

- Unlike AS 17, Ind AS 108 does not define terms such as segment revenue, segment profit or loss, segment assets and segment liabilities. As a result, diversity of reporting practices will increase.

- Since Ind AS 108 does not define segments as either business or geographical segments and does not require measurement of segment amounts based on an entity’s Ind AS accounting policies, an entity must disclose how
it determined its reportable operating segments, along with the basis on which disclosed amounts have been measured. These disclosures include reconciliations of the total key segment amounts to the corresponding entity amounts reported in Ind AS financial statements.

- A measure of profit or loss and assets for each segment must be disclosed. Additional line items, such as interest revenue and interest expense, are required to be disclosed if they are provided to the CODM (or included in the measure of segment profit or loss reviewed by the CODM). AS 17, in contrast, specifies the items that must be disclosed for each reportable segment.

- Under Ind AS, disclosures are required when an entity receives more than 10% of its revenue from a single customer. In such instances, an entity must disclose this fact, the total amount of revenue earned from each such customer and the name of the operating segment that reports the revenue. Disclosure is not required of the name of each major customer, nor the amounts of revenue reported in each segment for that customer.

Similar disclosures are not required under AS 17.

**Key impact**

**Identification of CODM**

Reporting under Ind AS 108 is based on information furnished to the CODM. The term CODM defines a function rather than an individual with a specific title. The function of the CODM is to allocate resources and assess operating results of the segments of an entity. The CODM could either be an individual, such as the chief executive officer, the chief operating officer, a group of executives such as the board of directors or a management committee. Entities should review their management structure to identify the CODM.

**Change in segment reporting approach**

On adoption of Ind AS 108, the identification of an entity’s segments may change from the position under AS 17. Ind AS 108 requires operating segments to be identified on the basis of internal reports on components of the entity that are regularly reviewed by the CODM, in order to allocate resources to the segment, and to assess its performance. AS 17 requires an entity to identify two sets of segments, business and geographical, using a risk-and-reward-approach, with the entity’s “system of internal financial reporting to key management personnel” serving only as the starting point for the identification of such segments.

**Goodwill impairment**

Ind AS 36 requires goodwill to be allocated to each CGU or to groups of CGUs. The relevant CGU or group of CGUs must represent the lowest level within the entity at which the goodwill is monitored for internal management purposes, and may not be larger than an operating segment. If different segments are reported under Ind AS 108, than were reported under AS 17, it follows that there will be differences between the CGUs that make up an Ind AS 108 segment and those that made up an AS 17 segment. As a result, the CGUs supporting goodwill may no longer be in the same segment under Ind AS 108 as under AS 17. It may, therefore, be necessary to reallocate goodwill associated with CGUs that are affected by the change from AS 17 to Ind AS 108. It is possible that this reallocation of goodwill could “expose” CGUs for which the carrying amount, including the allocated goodwill, exceeds the recoverable amount, thereby, giving rise to an impairment loss.

**Customer concentration**

On adoption of Ind AS, entities will be required to furnish a disclosure of customer concentration, which will enable investors to assess risk faced by a company. The company will have to compile information of revenue generated by each customer to furnish disclosures required by Ind AS 108.

**Reconciliation of management information system with financial statement**

Ind AS 108 requires segment reporting to be made based on information furnished to CODM. If the policies followed for computing information for management information system does not match with those used in financial statements, an entity will need to furnish reconciliation. Hence, entities need to devise or upgrade systems to prepare reconciliation between the MIS and the accounting system.
First-time adoption of Ind AS

First-time adoption challenges and perspective

Although, entities regularly adopt new accounting standards under Indian GAAP, adopting Ind AS which is an entirely different basis of accounting poses a distinct set of problems.

► The sheer magnitude of efforts involved in adopting a large number of new accounting standards,
► The requirements of individual Ind AS differ significantly from those under Indian GAAP, and
► Large amount of information that now needs to be collected for recognition, measurement and disclosure purposes that was not previously required under Indian GAAP.

In principle, a first-time adopter should prepare its Ind AS financial statements as if it had always applied Ind AS. However, this may not be possible to achieve in many cases. Ind AS 101 First-time Adoption of Indian Accounting Standards provides certain solutions in overcoming practical difficulties in applying Ind AS for the first time. Ind AS 101 provides the basis on which an entity will convert its previous financial statements to Ind AS. It prescribes ground rules and accounting policies to be followed in an entity's first set of Ind AS financial statements, and in preparation of its opening Ind AS balance sheet. The opening Ind AS balance sheet serves as the starting point for the future accounting under Ind AS.

Though Ind AS 101 goes some way to reduce the burden of historical accounting information, it does not turn the transition process into a hassle free job. Even under Ind AS 101, the transition process may remain complex and time consuming for many entities. It places demands on entities in areas such as staff training, data collection, analysis of contracts and other critical agreements, and new or modified information system requirements.

There are several important decisions which need to be made as part of Ind AS conversion. These decisions will affect the amount of work required on Ind AS adoption as well as financial results/financial position of a company both at the time of conversion as well as in the post-conversion period. While there are no right or wrong answers to the multitude of questions which need to be addressed on the first-time adoption, it is imperative that senior personnel of first-time adopters spend the time necessary to understand which combination of answers will yield the best result for their entity. Key choices to be made include:
Ind AS elections at date of transition: Ind AS 101 contains a number of voluntary exemptions that represent unique choices for a first-time adopter. Entities must evaluate which exemptions are relevant and which options offered within the exemptions lead to the best outcome for the entity. For example, if an entity elects the exemption to apply Ind AS 103 Business Combinations prospectively, there are clearly significantly less efforts involved because the entity will not be required to get retrospective fair valuation done for identifiable assets acquired and liabilities assumed and can largely continue with accounting done under the previous GAAP. However, consider that an entity has made a substantial business combination in the recent past years which resulted in considerable goodwill because it was required to recognize assets and liabilities acquired at book value under the Indian GAAP. In this case, retrospective application of Ind AS 103 will give the entity an opportunity to present true worth of the acquisition and reduce the amount of goodwill. Retaining goodwill at a substantial amount can cause huge P&L volatility because of impairment.

Selection of accounting policies: Under Ind AS, it is necessary to make certain accounting policy choices, and the choices made can have a significant impact on an entity’s financial results and the processes that support financial reporting. For example, is it more appropriate to recognize property, plant and equipment at cost or at fair value? If fair value is considered to be the better choice, how will the entity go about obtaining appropriate fair value information?

There is no “one size fits all” answer to these questions. Time and careful consideration are required to achieve an optimal end result.

Overview of Ind AS 101

Ind AS 101 is applicable to the first set of annual Ind AS financial statements prepared by an entity and to each interim financial report, if any, that it presents in accordance with Ind AS 34 Interim Financial Reporting, for part of the period covered by its first Ind AS financial statements.

The objective of Ind AS 101 is to ensure that an entity's first Ind AS financial statements, and its interim financial reports for part of the period covered by those financial statements, contain high quality information that:

a) Is transparent for users and comparable over all periods presented,

b) Provides a suitable starting point for accounting under Ind AS, and

c) Can be generated at a cost that does not exceed benefits to users.

Ind AS 101 prescribes the procedures that an entity is required to follow while adopting Ind AS for the first time. The underlying principle is that a first-time adopter should prepare financial statements as if it had always applied Ind AS. However, it establishes two types of departure from the principle of full retrospective application of Ind AS:

- It prohibits retrospective application of some aspects of other standards (mandatory exceptions), and

- It grants a number of exemptions from some of the requirements of other standards (voluntary exemptions).
Ind AS 101 is very much a rule-based standard, which can lead to different answers in similar situations and sometimes to counter-intuitive answers. To illustrate, in the case of compound financial instruments, Ind AS 101 requires retrospective application of Ind AS principles to determine the fair value of financial liability component at the time of initial recognition. This fair value is used to identify equity component and subsequent accounting for the liability component. A voluntary exemption is available only if the financial liability component is no longer outstanding at the date of transition to Ind AS.

In contrast, Ind AS 101 contains a mandatory exception for interest free/concessional loan from the government. A first-time adopter is generally not allowed to apply Ind AS requirement retrospectively to determine the fair value of loan at the date of initial recognition. Rather, previous GAAP carrying amount at the transition date is used as Ind AS carrying amount at the transition date.

In principle, determination of the fair value of financial liability component of compound financial instrument or that of government loan at the date of initial recognition involves similar principles. In both the cases, future cash flows need to be discounted at the market rate of interest. However, determining fair valuation of loan is required in the case of compound financial instrument, but prohibited in the case of interest free or concessional loan from the government. Ind AS 101 is clear that exemptions given and exceptions provided are applicable only to the specific items and cannot be applied by analogy to any other item.

Who is first-time adopter?

Ind AS 101 defines the “first Ind AS financial statements” as the first annual financial statements in which an entity adopts Ind AS by an explicit and unreserved statement of compliance with Ind AS notified under the Companies Act, 2013. The decisive factor is whether or not the entity made that explicit and unreserved statement of compliance with Ind AS.

Two interpretative issues that arise as a result of this requirement are discussed below.

An entity complies with all Ind AS but does not make an unreserved statement of compliance with Ind AS. Will those statements be treated as first Ind AS financial statements?

No, those financial statements will not be treated as first Ind AS financial statements. This scenario may lead to potential legal implications for companies as compliance with Ind AS is mandatory for all companies under the roadmap.

The entity does not comply with Ind AS but makes an unreserved statement of compliance with Ind AS (could be recognition, measurement or disclosure). The auditors have qualified the financial statements as not complying with Ind AS. Will those statements be treated as first Ind AS financial statements?

Yes, these financial statements will be treated as first Ind AS financial statements. In subsequent years, the entity can make the appropriate changes by applying Ind AS 8 Accountin Estimates and Errors to correct the errors.

An entity that presents its first Ind AS financial statements is a first-time adopter, and should apply Ind AS 101 in preparing those financial statements. It should also apply Ind AS 101 in each interim financial report that it presents in accordance with Ind AS 34 Interim Financial Reporting for a part of the period covered by its first Ind AS financial statements.

The roadmap issued by the MCA is clear that once a company opts to follow Ind AS either voluntarily or mandatorily, it cannot discontinue the same. Hence, a company can be first-time adopter of Ind AS and apply Ind AS 101 only once during its lifetime.
First-time adoption timeline/key dates

Two terms are key to understand Ind AS 101: reporting date and transition date. The reporting date is the end of the latest period covered by Ind AS financial statements or by an interim financial report. The transition date is the beginning of the earliest period for which an entity presents full comparative information under Ind AS in its first Ind AS financial statements.

To illustrate, consider an Indian company with a March year-end has net worth greater than INR500 crores. The company chooses not to use the early application choice and therefore needs to apply Ind AS for the financial year beginning on or after 1 April 2016. The company’s first mandatory reporting date under Ind AS will be 31 March 2017. In the financial statements for the year ended 31 March 2017, it also needs to present comparative Ind AS information for the year ended 31 March 2016. Consequently, its transition date to Ind AS will be 1 April 2015. In other words, its first set of financial statements will be for 1 April 2016 to 31 March 2017 with Ind AS comparative information also provided for 1 April 2015 to 31 March 2016. The opening Ind AS balance sheet date will be as of 1 April 2015.
Consistent application of accounting policies

Ind AS 101 requires an entity to prepare and present an opening Ind AS balance sheet at its transition date, i.e., 1 April 2015 in the above example. The opening Ind AS balance sheet is the starting point for subsequent accounting under Ind AS.

Ind AS 101 requires a first-time adopter to use the same accounting policies in its opening Ind AS balance sheet and for all periods presented in its first Ind AS financial statements. To achieve this, the entity should comply with each Ind AS effective at the end of its first Ind AS reporting period, after taking into account voluntary exemptions and mandatory exceptions to the retrospective application of Ind AS.

The requirement to apply same accounting policies to all periods prohibits a first-time adopter from applying previous versions of standards that were effective at earlier dates. This not only enhances comparability, but also gives users comparative information based on Ind AS that are superior to superseded versions of those standards and avoids unnecessary costs. For similar reasons, Ind AS 101 also permits an entity to apply a new Ind AS that is not yet mandatory if that standard allows early application. After the standard is selected, it is applied consistently throughout the periods presented.

Example 1

Background

The reporting date for FTA Limited’s first Ind AS financial statements will be 31 March 2017. Therefore, its date of transition to Ind AS is 1 April 2015. FTA presents financial statements under Indian GAAP annually to 31 March each year up to, and including, 31 March 2016.

Application of requirements

FTA will be required to apply the Ind AS effective for periods ending on 31 March 2017 in:

- Preparing and presenting its opening Ind AS balance sheet as at 1 April 2015, and
- Preparing and presenting its balance sheet for 31 March 2017 (including comparative amounts for 31 March 2016), statement of profit and loss, statement of changes in equity and cash flow statement for the year ended 31 March 2017 and disclosures (including comparative information for the year ended 31 March 2016)

If a new Ind AS is not yet mandatory but permits early application, FTA is permitted, but not required, to apply that Ind AS in its first Ind AS financial statements retroactive to 1 April 2015.

The fundamental principle of Ind AS 101 is to require full retrospective application of the standards in force at an entity’s reporting date, with limited voluntary exemptions and mandatory exceptions. The requirements of Ind AS 8 pertaining to change in accounting policies do not apply in an entity’s first Ind AS financial statements. Therefore, Ind AS 8 applies to entities subsequent financial statements.

If during the period covered by its first Ind AS financial statements an entity changes its accounting policies or its use of exemption contained in Ind AS, it will explain the changes between its first Ind AS interim financial report and its first Ind AS annual financial statements.
Previous GAAP

For the application of exemptions and exceptions as well as for disclosure of reconciliations required by Ind AS 101, the previous GAAP of first-time adopter is extremely relevant. Ind AS 101 defines “previous GAAP” as “the basis of accounting that a first-time adopter used for its statutory reporting in India immediately before adopting Ind AS. For instance, companies required to prepare their financial statements in accordance with section 133 of the Companies Act, 2013, will consider those financial statements as previous GAAP financial statements.”

In accordance with section 133 of the Companies Act, the GAAP permitted for standalone and consolidated financial statements is Indian GAAP. Even in the case of foreign subsidiaries, associates and joint ventures of an Indian company, for the purposes of preparing Ind AS CFS, the previous GAAP will generally be Indian GAAP.

Transition from Indian GAAP to Ind AS

In preparing the opening Ind AS balance sheet, subject to voluntary exemptions and mandatory exceptions, an entity should:

- **Not recognize items as assets or liabilities if Ind AS does not permit such recognition**
  
  Assets and liabilities recognized under Indian GAAP, which do not qualify for recognition under Ind AS, need to be eliminated from the opening Ind AS balance sheet. For example, proposed dividends cannot be disclosed as liability in Ind AS and this liability should be eliminated from the opening Ind AS balance sheet.

- **Recognize all assets and liabilities whose recognition is required by Ind AS**
  
  Some examples are:

  All derivative financial assets and liabilities and embedded derivatives requiring separation need to be recognized in the opening Ind AS balance sheet. If these are not recorded under Indian GAAP, entities need to bring them on the opening Ind AS balance sheet.

  Ind AS requires restructuring provisions to be recognized based on constructive obligation, while Indian GAAP permits recognizing such provision only when legal obligation arises. If a first-time adopter had constructive obligation on the transition date, it needs to recognize the provision in the opening Ind AS balance sheet. If there was no legal obligation by that date, the Indian GAAP balance sheet would not have recorded such provision.

  Ind AS 12 is based on the balance sheet approach. In contrast, AS 22 requires deferred taxes to be recognized based on the income statement approach. Hence, temporary differences, for which deferred tax is not recognized under Indian GAAP, need to be identified and recognized in the opening Ind AS balance sheet.

  An entity may not have prepared CFS under Indian GAAP or may not have consolidated a subsidiary which was excluded under AS 21. The opening Ind AS balance sheet needs to be drawn up to ensure all subsidiaries are consolidated in the consolidated opening Ind AS balance sheet.

  Entities also need to gather information, which is required to be disclosed in the Ind AS financial statements and was not disclosed under Indian GAAP. For example, Indian GAAP prohibits disclosure of contingent assets, whereas, Ind AS requires such disclosure.

  **Reclassify assets, liabilities and items of equity according to the requirements of Ind AS**

  Some common reclassifications are highlighted below:

  Under Indian GAAP, liability and equity classification is based on legal form, rather than economic substance. For example, all redeemable preference shares are classified as equity under Indian GAAP. Under Ind AS, liability vs. equity classification will be based on economic substance and definition of these terms. Consequently, a first-time adopter needs to identify items which meet the definition of equity and liability under Ind AS and reclassify them accordingly in the opening Ind AS balance sheet.

  Ind AS 101 provides an exemption from split accounting of compound financial instruments when certain conditions are satisfied. When this exemption cannot be availed, compound financial instruments need to be split into equity and liability portions for their appropriate classification.

  There may be acquired intangible assets in the past business combinations, which do not meet the definition of intangible assets under Ind AS. These need to be reclassified to goodwill.
Measure all assets and liabilities in accordance with Ind AS

All assets and liabilities need to be measured using Ind AS principles. For example, an entity will need to measure certain agricultural assets at fair value, which may not have been the measurement basis under Indian GAAP.

Any change in accounting policies on adoption of Ind AS may cause changes in the amounts previously recognized in respect of events and transactions that occurred before the date of transition. The effects of these changes should be recognized at the date of transition to Ind AS in retained earnings or, if appropriate, in another category of equity. For example, an entity that applies the Ind AS 16 - Property, Plant and Equipment - revaluation model in its first Ind AS financial statements would recognize the difference between cost and the revalued amount of property, plant and equipment in a revaluation reserve. By contrast, an entity that had applied a revaluation model under its previous GAAP, but decided to apply the cost model under Ind AS 16, would reallocate the revaluation reserve to retained earnings or a separate component of equity not described as a revaluation reserve.

A first-time adopter is under no obligation to ensure that its Ind AS accounting policies are similar to or as close as possible to its previous GAAP accounting policies. Therefore, a first-time adopter could adopt Ind AS 16 revaluation model despite the fact that it applied a cost model under its previous GAAP or vice versa. However, a first-time adopter would need to take into account the guidance in Ind AS 8 to ensure that its choice of accounting policy results in information that is relevant and reliable.

The requirement to prepare the opening Ind AS balance sheet and “reset the clock” at that date poses several challenges for first-time adopters. Even a first-time adopter that already applies a standard that is directly based on Ind AS may decide to restate items in the opening Ind AS balance sheet. To illustrate, consider that under Indian GAAP, an entity accounts for its items of property, plant and equipment at cost less depreciation. At the transition date, Indian GAAP carrying value of PPE is the same as that would have been arrived at by applying Ind AS 16 retrospectively. The entity may still decide to use deemed cost exemption for some or all of its assets as allowed by Ind AS 101.

As stated above, Ind AS 101 requires that effect of any change in accounting policy should be recognized at the date of transition to Ind AS in retained earnings. A company will identify distributable portion of retained earnings in accordance with the requirements of the Companies Act, 2013.
Departures from full retrospective application

Ind AS 101 establishes two types of departure from the principle of full retrospective application of standards in force at the end of the first Ind AS reporting period.

Mandatory exceptions

Ind AS 101 prohibits retrospective application of Ind AS 101 in some areas, particularly where this would require judgments by management about past conditions after the outcome of a particular transaction is already known. The mandatory exceptions in the standard cover the following situations:

- Estimates
- Classification and measurement of financial assets
- Impairment of financial assets
- Derecognition of financial assets and financial liabilities
- Embedded derivatives
- Hedge accounting
- Government loans
- Non-controlling interests

Voluntary exemptions

In addition to mandatory exceptions, Ind AS 101 grants limited voluntary exemptions from the general requirement of full retrospective application of the standards in force at the end of an entity's first Ind AS reporting period. These exemptions relate to:

- Business combination
- Share-based payment transactions
- Insurance contracts
- Deemed cost
- Leases
- Cumulative translation differences
- Investments in subsidiaries, joint ventures and associates
- Assets and liabilities of subsidiaries, associates and joint ventures
- Compound financial instruments
- Designation of previously recognized financial instruments
- Fair value measurement of financial assets or financial liabilities at initial recognition
- Decommissioning liabilities included in the cost of property, plant and equipment
- Service concession arrangements
- Extinguishing financial liabilities with equity instruments
- Severe hyperinflation
- Joint arrangements
- Stripping costs in the production phase of a surface mine
- Designation of contracts to buy or sell a non-financial item
- Revenue from contracts with customers, and
- Non-current assets held for sale and discontinued operations

Application of these exemptions is entirely optional, i.e., a first-time adopter can pick and choose the exemptions that it wants to apply. It is important to note that Ind AS 101 does not establish a hierarchy of exemptions. Therefore, when an item is covered by more than one exemption, a first-time adopter has a free choice in determining the order in which it applies exemptions. It is, however, specifically prohibited to apply these exemptions by analogy to other items. Moreover, in areas where there is no voluntary exemption, the entity cannot avoid applying Ind AS retrospectively on the argument that cost of complying with them is likely to exceed the benefits to users of financial statements.

For the purpose of this publication, we have divided exceptions and exemptions into suitable headings, such as, non-financial assets and liabilities, revenue, business combination and related items, financial instruments and other miscellaneous exemptions and exceptions.
Non-financial assets and liabilities

Deemed cost

Full retrospective application of Ind AS 16, Ind AS 38 and Ind AS 40 to the items of property, plant and equipment (PPE), intangible assets and investment property could be quite onerous because:

- These items are long-lived which means that accounting records for the period of acquisition may not be available anymore.
- The entity may have revalued items in the past as a matter of accounting policy,
- Even if the items were carried at depreciated cost, the accounting policy for recognition, measurement and depreciation may not have been Ind AS compliant.

Given the significance of items such as PPE in the balance sheet of many first-time adopters and the sheer number of transactions affecting PPE, restatement is not only difficult but would often also involve huge cost and effort. Nevertheless, a first-time adopter needs a starting point for those assets in its opening Ind AS balance sheet. Therefore, Ind AS 101 includes an exemption for “deemed cost” that may not be the “true” Ind AS compliant cost basis of an asset, but that is deemed to be a suitable starting point. When the exemption is applied, deemed cost is the basis for subsequent depreciation and impairment tests.

A full retrospective restatement according to Ind AS 16 is one of the basis for measuring PPE on first time adoption. However, to deal with practical issues in the retrospective restatement, Ind AS 101 permits a first-time adopter to measure items of PPE at deemed cost at the date of transition to Ind AS. If a first time adopter uses deemed cost exemption, subsequent depreciation/amortization of the asset is based on the deemed cost and starts from the date for which the entity established the deemed cost.

- Fair value/revaluation as deemed cost
- Event-driven fair value measurement as deemed cost
- Previous GAAP carrying value as deemed cost

a) Use of fair valuation or revaluation as deemed cost

Ind AS 101 permits a first-time adopter to measure individual items of PPE at deemed cost at the date of transition to Ind AS. Under this approach, the deemed cost that a first-time adopter uses is either:

1. The fair value of the item at the transition date, or
2. A revaluation under the previous GAAP at, or before the date of transition to Ind AS, if the revaluation was, at the date of the revaluation, broadly comparable to:
   - Fair value, or
   - Cost or depreciated cost under Ind AS, adjusted to reflect, for example, changes in a general or specific price index.

The revaluations referred to in (2) above need only be “broadly comparable” to fair value or reflect an index applied to a cost that is broadly comparable to cost determined under Ind AS. It appears that in the interest of practicality, Ind AS 101 allows flexibility in this matter.

Ind AS 101 describes revaluations referred to in (2) above as a “previous GAAP revaluation”. Therefore, in our view, such revaluations can only be used as the basis for deemed cost if they were recognized in the first-time adopter’s previous GAAP financial statements. For example, a previous GAAP impairment (or reversal of an impairment) that resulted in recognition of the related assets at fair value in the previous GAAP financial statements may be recognized as a previous GAAP revaluation for purposes of applying this exemption. However, when the previous GAAP impairment was determined for a group of impaired assets (i.e., a cash generating unit), the recognized value of an individual asset needs to have been broadly comparable to its fair value for the purposes of this exemption.

If the deemed cost of an asset was determined before the date of transition to Ind AS, then deemed cost forms the basis for the cost of the asset under Ind AS at the date the valuation was performed and not at the date of transition. Depreciation under Ind AS is determined from the date deemed cost is applied till the date of transition.

In addition to PPE, Ind AS 101 allows the above deemed cost exemption to be used for the categories of assets listed below:

- Investment property accounted for in accordance with the cost model in Ind AS 40, and
- Intangible assets meeting recognition criteria and criteria for revaluation under Ind AS 38 (they need to have an active market)
A first-time adopter cannot use the above mentioned deemed cost approach for any other asset or liability. The use of fair value or revaluation as deemed cost for intangible assets will be very limited in practice because of the definition of an active market in Ind AS 113 Fair Value Measurement. An active market is defined as one in which transactions for the item take place with sufficient frequency and volume to provide pricing information on an ongoing basis. Therefore, a first-time adopter will not be able to apply this exemption to most intangible assets.

It is important to note that the abovementioned deemed cost exemption in Ind AS 101 does not take classes or categories of assets as its unit of measure, but refers to “an item of PPE” and similarly for investment property and intangible assets. Ind AS 16 does not prescribe the unit of measure for recognition, i.e., what constitutes an item of PPE. Therefore, judgment is required in applying the recognition criteria to an entity’s specific circumstances. A first time adopter can, therefore, elect to apply this deemed cost exemption to only some of its assets. For example, it could elect to apply the exemption only to:

- A selection of properties
- Part of a factory, or
- Some of the assets leased under a single finance lease.

Example 2: Fair value as deemed cost

Background
FTA Limited is a pharmaceutical company, and its balance sheet contains items of PPE, purchased patents and borrowings. In an earlier year before transition to Ind AS, FTA has revalued its PPE to market value in its Indian GAAP financial statements. FTA also has some development projects in progress that meet the criteria in Ind AS 38 to be recognized as assets. FTA has recognized these costs as an intangible asset under Indian GAAP. Can management apply the fair value as deemed cost exemption to the development projects in progress?

Application of requirements
Management can apply the exemption to use fair value as deemed cost to the PPE only. If the Indian GAAP revaluation of PPE met the specified conditions, the fair value of these assets calculated in accordance with Indian GAAP can be used as deemed cost at the date of fair valuation. The purchased patents and development projects do not meet the criteria in Ind AS 38 for the revaluation of intangible assets, since there is no active market.

b) Event-driven fair value measurement as deemed cost
A first-time adopter may have established a deemed cost in accordance with previous GAAP for some or all of its assets and liabilities by measuring them at their fair value at one particular date because of an event such as a privatization or initial public offering. Ind AS 101 allows following exemptions in respect of such event-driven fair values:

(i) If the measurement date is at or before the date of transition to Ind AS, the entity may use such event-driven fair value measurements as deemed cost for Ind AS at the date of that measurement.

(ii) If the measurement date is after the date of transition to Ind AS, but during the period covered by the first Ind AS financial statements, the event-driven fair value measurements may be used as deemed cost when the event occurs. An entity should recognize the resulting adjustments directly in retained earnings (or if appropriate, another category of equity) at the measurement date.

Ind AS 101 describes these revaluations as “deemed cost in accordance with previous GAAP”. Therefore, to the extent that they related to an event that occurred prior to its date of transition or during the comparative period presented under Ind AS, they can only be used as the basis for deemed cost if they were recognized in the first-time adopter’s previous GAAP financial statements.

The “fair value or revaluation as deemed cost” exemption discussed above, only applies to items of PPE, investment property and certain intangible assets. The event-driven deemed cost exemption may be applied selectively to some or all assets and liabilities of a first time adopter.

Although a first-time adopter may use an event-driven fair value measurement as deemed cost for any asset or liability, it does not have to use them for all assets and liabilities that were revalued as a result of the event.

c) Use of Indian GAAP carrying amount as deemed cost
A first-time adopter may opt to continue with the carrying value for all of its PPE as recognized in its previous GAAP financial statements and use that as its deemed cost at the transition date. However, the entity should make necessary adjustments for decommissioning liabilities to be included in the carrying value of PPE. The following key points are to be noted for this option:
a) The option is available only where there is no change in the functional currency of the entity on the date of transition to Ind AS.

b) The option if elected needs to be applied to all items of PPE. Unlike “fair value as deemed cost” exemption, this exemption cannot be applied on item-by-item basis.

c) If the previous GAAP financial statements are Indian GAAP CFS, the previous GAAP amount of the subsidiary should be the Indian GAAP amounts used in preparing and presenting Indian GAAP CFS.

d) Where a subsidiary was not consolidated under previous GAAP, the amount required to be reported by the subsidiary according to the previous GAAP in its individual financial statements should be the previous GAAP amount.

e) Consider that a US subsidiary was not consolidated under Indian GAAP because it did not satisfy control criteria according to AS 21. Under Ind AS, such subsidiary will be consolidated based on definition of control given in Ind AS 110. For purpose of deemed cost exemptions, the fixed asset amounts recognized by the US subsidiary under its previous GAAP will be used.

f) This option can also be availed for intangible assets and investment property.

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Example 3: Practical issue in interaction with exemption for past business combinations

**Background**

In accordance with Ind AS 101, a first-time adopter may choose to restate all past business combinations or combinations occurring after a chosen date. If a first-time adopter restates any business combination to comply with Ind AS 103 Business Combinations, it needs to restate all later business combinations.

Consider that an entity, whose date of transition to Ind AS is 1 April 2015, decides to use Ind AS 101 exemption for continuing its PPE at previous GAAP carrying amount. The entity had acquired a subsidiary in 2013. The acquisition constitutes a business combination under Ind AS 103. The entity also decides to use business combination exemption in a manner to restate all combinations occurring after 1 January 2013. The relevant information regarding subsidiary’s PPE at 1 April 2015 is given below:

- Previous GAAP carrying value used for consolidation: INR120 million
- Fair value at the acquisition date: INR180 million
- Written down value (acquisition date fair value less cumulative depreciation upto transition date): INR165 million

At what amount should the entity recognize the PPE of the subsidiary in its Ind AS opening balance sheet?

**Application of requirements**

There is an apparent conflict between the two exemptions. The exemption relating to business combination used by the entity requires it to use the fair value of the PPE as of the acquisition date as cost to arrive at the transition date value. Therefore, the entity should recognize the PPE of subsidiary at INR165 million. The PPE exemption requires that for all items of PPE, the amount recognized in the Indian GAAP CFS will be carried forward, without any adjustment (except decommissioning cost). Therefore, the entity should recognize the PPE of the subsidiary at INR120 million. There is a conflict between the two exemptions. As a result of this conflict, three views seem possible: (a) PPE exemption will override the business combination exemption, (b) business combination exemption will override the PPE exemption, or (c) the two exemptions are not mutually exclusive and hence entities have a free choice on using either the PPE exemption or the business combination exemption. Till the time the MCA or the ICAI provide any further guidance to resolve this issue, a first-time adopter may be able to select one of these views as the accounting policy in preparing its opening Ind AS balance sheet. The view once selected should not be changed.
The “use of Indian GAAP carrying amount as deemed cost” exemption for PPE, investment property and intangible asset may reduce the quantum of conversion efforts required at the transition date. However, it may be noted that this particular exemption does not exist under IASB IFRS. Hence, if an entity decides to use this exemption, it will depart from IASB IFRS.

Decommissioning liabilities included in the cost of PPE

In accordance with Ind AS 16, the cost of an item of PPE includes the initial estimate of costs of dismantling and removing the item and restoring the site on which it is located, the obligation for which is incurred either when the item is acquired or as a consequence of having used the item during a particular period for purposes other than to produce inventories during that period. Therefore, a first-time adopter needs to ensure that PPE cost includes decommissioning provision determined in accordance with Ind AS 37 Provisions, Contingent Liabilities and Contingent Assets.

Appendix A to Ind AS 16 requires specified changes in a decommissioning, restoration or similar liability to be added to or deducted from the cost of the asset to which it relates; the adjusted depreciable amount of the asset is then depreciated prospectively over its remaining useful life. To apply these requirements retrospectively, a first-time adopter will need to construct historical records of all such adjustments that should have been made in the past. This may not be practicable in all the cases. To address these practical difficulties, Ind AS 101 allows an exemption whereby a first-time adopter may elect for such liabilities incurred before the date of transition, to:

a) Measure the liability at the date of transition to Ind AS in accordance with Ind AS 37,

b) Estimate the amount that would have been included in the cost of the related asset when the liability first arose, by discounting the liability to that date using its best estimate of the historical risk-adjusted discount rate(s) that would have applied for that liability over the intervening period, and

c) Calculate the accumulated depreciation on that amount, as at the transition date, on the basis of the current estimate of the useful life of the asset, using the entity’s Ind AS depreciation policy.
Example 4: Decommissioning liability

Background
FTA Limited’s date of transition to Ind AS is 1 April 2015. It has built a plant that was completed and ready for use on 1 April 2010. The facts relevant to the plant are summarized below:

<table>
<thead>
<tr>
<th>Description</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>Cost</td>
<td>INR1,400</td>
</tr>
<tr>
<td>Residual value</td>
<td>INR200</td>
</tr>
<tr>
<td>Economic life</td>
<td>20 years</td>
</tr>
<tr>
<td>Original estimate of decommissioning cost to be incurred</td>
<td>INR75</td>
</tr>
<tr>
<td>Revised estimate at 1 April 2015 of decommissioning cost</td>
<td>INR300</td>
</tr>
<tr>
<td>Discount rate applicable (assumed to be constant)</td>
<td>5.65%</td>
</tr>
<tr>
<td>Discounted value of original decommissioning liability on 1 April 2010</td>
<td>INR58</td>
</tr>
<tr>
<td>Discounted value of revised decommissioning liability on 1 April 2010</td>
<td>INR100</td>
</tr>
<tr>
<td>Discounted value of revised decommissioning liability on 1 April 2015</td>
<td>INR131</td>
</tr>
</tbody>
</table>

Assume that FTA Limited is not accounting for decommissioning liability under Indian GAAP.

Application of requirements
Full retrospective application of Appendix A to Ind AS 16 will require FTA Limited to go back in time and account for each revision of the decommissioning provision. Keeping in view practical difficulties, Ind AS 101 allows the following treatment to be followed:

Recognize decommissioning liability based on discounted value of revised liability on 1 April 2015, i.e., INR131

Amount to be added to cost of plant

Discounted value of revised decommissioning liability on 1 April 2010 = INR100

Accumulated depreciation on the above amount = INR100 x 5/20 = INR25

Net amount to be capitalized = INR100 - 25 = INR75

Entry to be passed

| Debit Plant         | INR75 |
| Debit Retained earnings | INR56 |
| Credit Decommissioning liability | INR131 |
In the example above, carrying value of the plant at the opening balance sheet date may have been determined either using or not using the fair value as deemed cost exemption. An entity, which has used the fair value as deemed cost option and elects to use the decommissioning liabilities exemption, should be aware that the interaction between these exemptions may lead to a potential overstatement of the underlying asset. To address this issue, a first-time adopter should assess whether the fair value of the asset is inclusive or exclusive of the decommissioning obligation and make necessary adjustment to remove the potential overstatement.

**Leases**

**Identification of embedded leases**

AS 19 Leases does not provide any specific guidance to determine whether an arrangement in substance conveys right to use an asset. Hence, under Indian GAAP, lease accounting is normally applied to transactions, which are structured as lease.

Appendix C to Ind AS 17 Determining whether an Arrangement contains a Lease prescribes specific principles for identifying leases contained in an arrangement, comprising a transaction or a series of related transactions, which does not take the legal form of a lease but conveys a right to use an asset. In accordance with Appendix C to Ind AS 17, the determination whether an arrangement contains a lease is made at the inception of the arrangement, which is the earlier of the date of the arrangement and the date of commitment by the parties to the principal terms of the arrangement. If a first-time adopter has entered into an arrangement potentially containing lease several years back, the entity is likely to face significant practical difficulties in going back, potentially many years, and making a meaningful assessment of whether the arrangement satisfied the criteria at that time. To address practical difficulties, Ind AS 101 states that a first-time adopter can elect to make this assessment as of the date of transition based on the facts at that date, rather than at inception of the arrangement. In other words, a first-time adopter may assess arrangements existing as of the date of transition to Ind AS to determine if the arrangements contain a lease on the basis of facts and circumstances as of the date of transition, as opposed to facts and circumstances as of date of inception or modification of arrangements.

Ind AS 101 also recognizes that in some cases, a first time adopter may make the same determination of whether an arrangement contained a lease in accordance with previous GAAP as that required by Appendix C to Ind AS 17. However, this assessment is made at a date other than the date required by Appendix C to Ind AS 17. In such cases, the first-time adopter is not required to reassess that determination when it adopts Ind AS. However, this option can be used only if the assessment made under the previous GAAP would have given the same outcome as that resulting from applying Ind AS 17 and its Appendix C.

This voluntary exemption only applies to the assessment of whether an arrangement contains a lease. If an arrangement is determined to contain a lease, a first-time adopter applies Ind AS 17 to determine the classification of the lease as an operating or finance lease, from the inception of the arrangement.

**Land leases**

Since AS 19 did not contain any specific guidance on accounting for land leases, Indian entities were accounting for such leases in different ways under Indian GAAP. In contrast, Ind AS 17 requires a lease of land to be assessed as an operating or finance lease, based on the same criteria that are applicable for lease of other assets. Ind AS 17 also states that when a lease includes both land and building elements, an entity assesses the classification of each element as finance or an operating lease separately in accordance with the criteria laid in the standard. In determining whether the land element is an operating or a finance lease, an important consideration is that land normally has an indefinite economic life.

Ind AS 101 does not require Ind AS 17 to be applied retrospectively to land leases and it allows a voluntary exemption on the matter. In accordance with the exemption, when a lease includes both land and building elements, a first time adopter may assess the classification of each element as finance or an operating lease at the date of transition to Ind AS on the basis of facts and circumstances existing as at that date. If there is any land lease newly classified as finance lease at the transition date, which was classified differently under previous GAAP, then the first time adopter may recognize assets and liability at fair value on that date; and any difference between those fair values is recognized in retained earnings.
Service concession arrangements

As stated above, Appendices C to Ind AS 115 requires that infrastructure within its scope should not be recognized as property, plant and equipment of the operator, since the asset is “controlled” by the grantor. Instead, the operator recognizes a financial asset to the extent that it has an unconditional right to receive consideration from the grantor or the grantor has guaranteed the operator’s cash flow. The operator recognizes an intangible asset to the extent it has a right to charge users of the public service.

Ind AS 101 requires that a first-time adopter should apply Appendix C to Ind AS 115 retrospectively. However, in some cases, it may so happen that it is not practical to apply the requirements of Appendix C to Ind AS 115, retrospectively, e.g., because it is not practical to determine the fair value of construction and other services, which were rendered in the past. In such cases, Ind AS 101 gives first-time adopters a voluntary exemption to apply the following treatment:

- Recognize financial and intangible assets that existed at the date of transition to Ind AS
- Use the previous carrying amounts as the carrying amount at that date (no matter how they were previously classified), and
- Test the financial and intangible assets recognized at that date for impairment.

Hence, a first-time adopter will not be required to apply measurement requirements of Appendix C to Ind AS 115, retrospectively; however, it will still be required to apply classification requirements retrospectively. Moreover, unlike most of other exemptions, this exemption is applicable only to those arrangements where retrospective application is not practical. This exemption should not be treated as a free choice. There will be a high hurdle for companies to claim practicality as a means to avoid retrospective application. This decision is made for each arrangement separately.

Amortization of toll roads

Under Indian GAAP, Schedule II to the Companies Act, 2013, allows revenue based amortization for toll roads created under a service concession arrangement. Considering this, certain Indian companies amortize their toll roads using revenue-based amortization.

Ind AS 38 prohibits use of revenue based amortization method. For companies which have used revenue based amortization under Indian GAAP, Ind AS 101 read with Ind AS 38 gives an option to continue revenue based amortization for toll roads recognized in the financial statements for the period immediately before the beginning of the first Ind AS financial statements. However, such amortization will not be allowed for any new toll road arising from service concession arrangements entered into after the beginning of the first Ind AS reporting period.

Consider that a company will apply Ind AS for the first time in its financial statements for the year ended 31 March 2017. Its date of transition is 1 April 2015 and its last Indian GAAP financial statements were prepared for the year ended 31 March 2016. For any toll road recognized on or before 31 March 2016, the company has the option of continuing revenue based amortization. It should be noted that this is an option. In other words, a company is free to use Ind AS 38 for amortization. For any new toll arising from the service concession arrangements entered into after 1 April 2016, revenue based amortization will not be allowed. Rather, the company has to mandatorily apply Ind AS 38 for amortization.

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3 Please also refer the booklet titled “IFRS-converged Indian Accounting Standards - Outreach meeting dated 15 January 2015”, published by the Accounting Standards Board of the ICAI.
Revenue

Ind AS 115 *Revenue from Contracts with Customers* sets out principles that an entity applies to report useful information about the amount, timing, and uncertainty of revenue and cash flows arising from its contracts to provide goods or services to customers. The core principle requires an entity to recognize revenue to depict the transfer of goods or services to customers in an amount that reflects the consideration that it expects to be entitled to in exchange for those goods or services.

Ind AS 115 is a significant change from current Indian GAAP. Although it provides more detailed application guidance, entities will need to use more judgment in applying its requirements, in part, because the use of estimates is more extensive. The potential changes to revenue recognition for some entities may be significant.

Ind AS 101 gives voluntary exemption whereby a first-time adopter may use one or more of the following practical expedients when applying Ind AS 115 retrospectively:

1. For completed contracts, an entity need not restate contracts that begin and end within the same annual reporting period.
2. For completed contracts that have variable consideration, an entity may use the transaction price at the date the contract was completed rather than estimating variable consideration amounts in the comparative reporting periods, and
3. For all reporting periods presented before the beginning of the first Ind AS reporting period, an entity need not disclose the amount of the transaction price allocated to the remaining performance obligations and an explanation of when the entity expects to recognize that amount as revenue.

Entities may elect to apply none, some or all of these expedients. However, if an entity elects to use any of them, it must apply that expedient consistently to all contracts within all periods presented. In addition, entities are required to disclose the following information:

a) The expedients that have been used; and

b) To the extent reasonably possible, a qualitative assessment of the estimated effect of applying each of those expedients.

A first-time adopter is not required to restate contracts that were completed before the earliest period presented. A completed contract is a contract for which the entity has transferred all of the goods or services identified in accordance with previous GAAP.

Business combinations and consolidation

Accounting for business combinations under Ind AS is significantly different from that required under Indian GAAP. Retrospective application of Ind AS 103 to past business combinations may not be practical in all cases. Consider that an Indian company acquired a subsidiary almost 10 years back. Under Indian GAAP, as required by AS 21 *Consolidated Financial Statements*, the company recognized assets and liabilities of the subsidiary at book value. To apply Ind AS 103 retrospectively, the parent company will need to go back in the history and determine acquisition date fair values of assets and liabilities of the subsidiary. Considering the long-period of time, this may be impractical.

Against this background, besides deemed cost exemption for PPE, business combinations exemption in Ind AS 101 is probably the most significant exemption. It provides a first-time adopter an exemption from restating business combinations prior to its date of transition to Ind AS.

Business combinations prior to the transition date

A first-time adopter must account for any business combination occurring after its date of transition under Ind AS 103, i.e., any business combinations during the comparative periods need to be restated in accordance with Ind AS. An entity may elect not to apply Ind AS 103 to business combinations occurring before the date of transition. However, if a first-time adopter does restate a business combination occurring prior to its date of transition to comply with Ind AS 103, it must also restate any subsequent business combinations under Ind AS 103 and apply Ind AS 110 *Consolidated Financial Statements* from that date onwards. In other words, as shown on the time line below, a first-time adopter is allowed to choose any date in the past from which it wants to account for all business combinations under Ind AS 103 without having to restate business combinations that occurred prior to such date.
This exemption is available to all the transactions that meet definition of a business combination under Ind AS 103, irrespective of their classification under the previous GAAP. However, if the past acquisition is only an asset acquisition and not a business combination under Ind AS 103, this exemption does not apply. Rather, the acquirer may consider applying other applicable optional exemptions.

A first time adopter may even decide to apply Ind AS 103 retrospectively to all past business combinations. Neither Ind AS 103 nor Ind AS 101 prohibits such retrospective application. However, a first-time adopter should consider whether retrospective application of Ind AS 103 requires undue use of hindsight. If so, it may be advisable to avoid retrospective application of Ind AS 103 beyond a date when the first-time adopter can get information to apply Ind AS 103 without undue use of hindsight. Ind AS 101 prohibits use of hindsight.

Business combination exemption also applies to past acquisitions of associates, interests in joint ventures and interests in joint operations. Therefore, a first-time adopter taking advantage of the exemption will not have to revisit past business combinations, acquisitions of associates and joint ventures to establish fair values and amounts of goodwill/capital reserve under Ind AS. However, application of the exemption may be complex, and certain adjustments to transactions under the previous GAAP may still be required. When the exemption is applied:

- Classification of the combination as an acquisition, reverse acquisition or a pooling of interests does not change. As long as the transaction is a business combination within the scope of Ind AS 103, the previous GAAP accounting would be eligible to be carried forward with specific adjustments.
- In the opening Ind AS balance sheet, a first-time adopter should recognize all assets acquired and liabilities assumed in a past business combination, with the exception of:
  - Certain financial assets and liabilities that were derecognized and fall under the derecognition exception (refer Financial Instruments section), and
  - Assets (including goodwill) and liabilities that were not recognized in the acquirer's consolidated balance sheet under the previous GAAP and that would not qualify for recognition under Ind AS in the individual balance sheet of the acquiree. For instance, the acquirer did not recognize the acquiree's internally developed brand as a separate intangible asset under the previous GAAP. The acquirer does not recognize the brand in its opening Ind AS balance sheet since Ind AS 38 does not allow acquiree to recognize it as an asset in its separate Ind AS balance sheet. Consequently, any value attributable to the brand remains subsumed in goodwill in the acquirer’s opening Ind AS balance sheet.

<table>
<thead>
<tr>
<th>Date of transition to Ind AS</th>
<th>Beginning of first Ind AS reporting</th>
<th>Ind AS Reporting date</th>
</tr>
</thead>
</table>

Opening Ind AS balance sheet
The first-time adopter should recognize any resulting change by adjusting retained earnings (or, if appropriate, another category or equity), unless the change results from the recognition of an intangible asset previously subsumed in goodwill.  

If a first-time adopter has recognized certain items as assets/liabilities under the previous GAAP which do not qualify for recognition under Ind AS, it should exclude those items from its opening Ind AS balance sheet. An intangible asset, acquired as part of a business combination, which does not qualify for recognition as an asset under Ind AS 38 should be derecognized, with the related deferred tax and NCI, with an offsetting change to goodwill (unless the entity previously deducted goodwill directly from equity under its previous GAAP) or capital reserve (to the extent not exceeding the balance available in that reserve). All other changes resulting from derecognition of such assets and liabilities should be accounted for as adjustments of retained earnings or another category of equity, if appropriate. For example, any restructuring provisions recognized under the previous GAAP and which remain at the Ind AS transition date will need to be assessed against the Ind AS recognition criteria. If the criteria are not met, then the provisions must be reversed against retained earnings.

For assets and liabilities that are accounted for on a cost basis under Ind AS, the carrying amount in accordance with the previous GAAP of assets acquired and liabilities assumed in that business combination is their deemed cost immediately after the business combination. This deemed cost is the basis for cost-based depreciation or amortization from the date of the business combination.

Ind AS requires subsequent measurement of some assets and liabilities on a basis that is not based on the original cost, for example, investment in equity shares and derivative instruments are measured at fair value. The first-time adopter should measure these assets and liabilities on that basis in its opening Ind AS balance sheet, even if they were acquired or assumed in a past business combination. It should recognize any resulting change in the past carrying amount by adjusting retained earnings (or, if appropriate, another category of equity), rather than goodwill.

An asset acquired or a liability assumed in a past business combination may not have been recognized under the previous GAAP. However, this does not mean that such items have a deemed cost of zero in the opening Ind AS balance sheet. Instead, the acquirer recognizes and measures those items in its opening Ind AS balance sheet on the basis that Ind AS will require in the balance sheet of the acquiree.

Consider that the acquirer had not, in accordance with its previous GAAP, capitalized finance leases acquired in a past business combination. It should capitalize those leases in its consolidated financial statements. This is done on the same basis as Ind AS 17 Leases will require the acquiree to do in its Ind AS balance sheet.

**Example 5: Contingent liability not recognized under previous GAAP**

FTA Limited has acquired B Limited before date of transition to Ind AS. In its consolidated balance sheet, FTA did not recognize a contingent liability that still exists at the date of transition to Ind AS.

FTA should assess whether Ind AS 37 Provisions, Contingent Liabilities and Contingent Assets requires its recognition in the financial statements of the acquiree (B Limited) at the transition date. If so, FTA should recognize that contingent liability at the date of transition to Ind AS. However, if B Limited is not allowed to recognize the liability under Ind AS 37 because outflow is not probable, contingent liability is not recognized in the opening Ind AS balance sheet of FTA. This is despite the fact that on the application of Ind AS 103, FTA would have been required to recognize the contingent liability.
If a first time adopter recognizes assets acquired and liabilities assumed in past business combinations that were not recognized under the previous GAAP, the change resulting from the recognition should be accounted for as an adjustment of retained earnings or another category of equity, if appropriate. However, if the change results from the recognition of an intangible asset that was previously subsumed in goodwill, it should be accounted for as an adjustment of that goodwill.

A first-time adopter takes the carrying amount of goodwill under the previous GAAP at the date of transition to Ind AS as a starting point and only adjusts it as follows:

- Goodwill is increased by the carrying amount of any intangible asset acquired in a business combination under the previous GAAP (less any related deferred tax and NCI), that does not meet Ind AS recognition criteria.

- Goodwill is decreased if a first-time adopter is required to recognize an intangible asset that was subsumed in goodwill under the previous GAAP. It adjusts deferred tax and NCI accordingly.

- Goodwill must be tested for impairment at the date of transition to Ind AS in accordance with Ind AS 36 Impairment of Assets regardless of whether there is any indication that the goodwill may be impaired. Any resulting impairment loss is recognized in retained earnings unless Ind AS 36 requires it to be recognized in a revaluation surplus.

Ind AS 101 prohibits restatement of goodwill for most other adjustments reflected in the opening Ind AS balance sheet. Therefore, a first-time adopter electing not to apply Ind AS 103 retrospectively is not permitted to make any adjustments to goodwill other than those described above. For example, a first-time adopter cannot restate the carrying amount of goodwill:

- To exclude in-process research and development acquired in that business combination (unless the related intangible asset would qualify for recognition in accordance with Ind AS 38 in the balance sheet of the acquiree)

- To adjust previous amortization of goodwill

- To reverse adjustments to goodwill that Ind AS 103 would not permit, but were made under the previous GAAP because of adjustments to assets and liabilities between the date of the business combination and the date of transition to Ind AS.
Example 6: Application of business combinations exemption

FTA Limited (FTA) prepares its first Ind AS financial statements with reporting date of 31 March 2017 and comparative information of the year ended 31 March 2016 only. FTA’s date of transition to Ind AS is 1 April 2015. On 1 September 2013, FTA had acquired 100% of subsidiary XYZ. Under Indian GAAP, FTA:

- Classified the business combination as an acquisition by FTA
- Measured the assets acquired and liabilities assumed at the following amounts under Indian GAAP at 1 April 2015 (date of transition to Ind AS):
  - Property, plant and equipment — INR400 (under Indian GAAP); on 1 September 2013: INR500 (under Indian GAAP)
  - FVTOCI Investments — INR200 (Market value: INR600)
  - Pension liability — Nil (Ind AS 19 net liability: INR60)
  - Unamortized VRS expenses — INR50
  - Goodwill — INR360

In the opening (consolidated) Ind AS balance sheet, FTA decides to use business combination exemption whereby it will not restate the past combination. Accordingly, FTA:

- Classifies the business combination as an acquisition by FTA, even if it would have qualified under Ind AS 103 as reverse acquisition by the subsidiary XYZ.
- Does not adjust the accumulated amortization of goodwill under Indian GAAP. FTA tests goodwill for impairment under Ind AS 36 and recognizes any resulting impairment loss.
- Measures property, plant and equipment which require cost based measurement after acquisition at carrying amount under Indian GAAP immediately after business combination as their deemed cost. The asset will be stated at INR500 on 1 September 2013. The 1 April 2015 value is derived using Ind AS accounting from 1 September 2013 to 31 March 2015 for PPE on the balance of INR500. FTA may use further exemptions that are available for PPE at the transition date.
- Measures FVTOCI investments at fair value of INR600 and adjusts the corresponding effect in equity as a gain on investments (INR400).
- Recognizes a pension liability at INR60 with a corresponding debit/credit to retained earnings.
- Writes off unamortized VRS expenditure with a corresponding debit to retained earnings.
- Tests assets for impairment, if there is any indication that identifiable assets are impaired, based on conditions that existed at the date of transition to Ind AS.
If the first-time adopter recognized goodwill in accordance with the previous GAAP as a deduction from equity:

- It should not recognize that goodwill in its opening Ind AS balance sheet. Furthermore, it should not reclassify that goodwill to profit or loss if it disposes of the subsidiary or if the investment in the subsidiary becomes impaired.
- Adjustments resulting from the subsequent resolution of a contingency affecting the purchase consideration will be recognized in retained earnings.
- The measurement of NCI and deferred tax follows from the measurement of other assets and liabilities. Therefore, the above adjustments to recognized assets and liabilities affect NCI and deferred tax.

**Transition accounting for contingent consideration**

Business combination exemption under Ind AS 101 does not extend to contingent consideration that arose from a transaction that occurred before the transition date, even if the acquisition itself is not restated due to the use of the exemption. Therefore, such contingent consideration is recognized at its fair value at the transition date, regardless of the accounting under the previous GAAP. If contingent consideration was not recognized at fair value at the date of transition under the previous GAAP, the resulting adjustment is recognized in retained earnings or other category of equity, if appropriate. Subsequent adjustments will be recognized following the provisions of Ind AS 103.

**Previously unconsolidated subsidiaries**

Under the previous GAAP, a first-time adopter may not have consolidated a subsidiary acquired in a past business combination. For example, this may be the case because the parent did not regard it as a subsidiary under the previous GAAP or it did not prepare CFS. A first-time adopter applying the business combinations exemption should adjust the carrying amounts of the subsidiary’s assets and liabilities to the amounts that Ind AS would require in the subsidiary’s balance sheet. The deemed cost of goodwill equals the difference at the date of transition to Ind AS between:

a) The parent’s interest in those adjusted carrying amounts, and
b) The cost in the parent’s separate financial statements of its investment in the subsidiary.

This exemption requires a first-time adopter to compare the parent’s share in net assets of subsidiary at transition date with the carrying value of the investment in its separate financial statements prepared using Ind AS 27. This is no more than a pragmatic “plug” that facilitates the consolidation process but does not represent the true goodwill that might have been recorded if Ind AS had been applied to the original business combination.

If a first-time adopter, in its separate financial statements, does not opt to measure its cost of investment in a subsidiary at its transition date fair value, the deemed cost of the goodwill is calculated by comparing the original cost of the investment to its share of the carrying amount of the net assets determined on the transition date. This could give rise to negative goodwill/ minimal goodwill, in case of a profitable subsidiary. Moreover, the subsidiary’s past dividend distribution may impact the deemed cost of goodwill.

This exemption does not apply to previously unconsolidated subsidiaries which the parent did not acquire in a business combination, but established them. Ind AS 101 does not provide any specific guidance on such cases. However, implementation guidance to IFRS 1 states that if the parent did not acquire a previously unconsolidated subsidiary, it does not recognize goodwill in relation to those subsidiaries. Any difference between the carrying amount of the subsidiary and the net identifiable assets as determined above would be treated as an adjustment to retained earnings, representing the accumulated profits or losses that would have been recognize as if the subsidiary had always been consolidated. We believe that the position stated under IFRS 1 is correct for previously unconsolidated subsidiaries, which the parent did not acquire, but established them. Hence, this guidance under IFRS 1 should apply under Ind AS also.
Previously consolidated entities that are not subsidiaries

A first-time adopter may have consolidated an investment under the previous GAAP that does not meet the definition of a subsidiary under Ind AS. In such a case, the first time adopter should first determine the appropriate classification of investment under Ind AS and apply the first-time adoption rules in Ind AS accordingly. For example, such previously consolidated investments may be accounted for as either:

- An associate or a joint venture: If it is determined that an investment should be accounted for using the equity method of accounting as described in Ind AS 28 Investments in Associates and Joint Ventures, the first-time adopter applying the business combinations exemption should also apply that exemption to past acquisitions of investments in associates/joint ventures. If the business combinations exemption is not applicable or the entity did not acquire the investment in the associate or joint venture, Ind AS 28 should be applied retrospectively.
- An investment under Ind AS 109 if it is determined that an investment is not a subsidiary, associate, or joint venture, or
- An executory contract or service concession arrangement: there are no first-time adoption exemptions that apply; therefore, Ind AS should be applied retrospectively.

Currency adjustments to goodwill

Ind AS 21 The Effects of Changes in Foreign Exchange Rates requires that any goodwill arising on the acquisition of a foreign operation and any fair value adjustments to the carrying amounts of assets and liabilities arising on the acquisition of that foreign operation should be treated as assets and liabilities of the foreign operation. For a first-time adopter, it may be impracticable, especially after corporate restructuring, to determine retrospectively the currency in which goodwill and fair value adjustments should be expressed.

To address these practical challenges, Ind AS 101 contains a voluntary exemption whereby a first-time adopter need not apply this requirement of Ind AS 21 retrospectively to fair value adjustments and goodwill arising in business combinations that occurred before the date of transition to Ind AS. If Ind AS 21 is not applied retrospectively, a first-time adopter should treat such fair value adjustments and goodwill as assets and liabilities of the entity rather than as assets and liabilities of the acquiree. Therefore, those goodwill and fair value adjustments are either already expressed in the entity’s functional currency or are non-monetary foreign currency items, which are reported using the exchange rate applied under the previous GAAP.

If a first-time adopter chooses not to take the exemption mentioned above, it must apply Ind AS 21 retrospectively to fair value adjustments and goodwill arising in either:

- All business combinations that occurred before the date of transition to Ind AS, or
- All business combinations that the entity elects to restate to comply with Ind AS 103.

Assets and liabilities of subsidiaries, associates and joint ventures

Subsidiary becomes a first-time adopter later than its parent

If a subsidiary becomes a first-time adopter later than its parent, it should, in its financial statements, measure its assets and liabilities at either:

- The carrying amounts that would be included in the parent’s CFS, based on the parent’s date of transition to Ind AS, if no adjustments were made for consolidation procedures and for the effects of the business combination in which the parent acquired the subsidiary. However, this election is not available to a subsidiary of an investment entity, as defined in Ind AS 110, or
- The carrying amounts required by the rest of Ind AS 101, based on the subsidiary’s date of transition to Ind AS. These carrying amounts could differ from those described above:
  - When the exemptions in Ind AS 101 result in measurements that depend on the date of transition to Ind AS.
  - When accounting policies used in the subsidiary’s financial statements differ from those in the CFS. For example, the subsidiary may use as its accounting policy the cost model in Ind AS 16, whereas, the group may use the revaluation model.
If a subsidiary was acquired after the parent’s date of transition to Ind AS, then it cannot apply the first option because there are no carrying amounts included in the parent’s CFS, based on the parent’s date of transition.

A similar election is available to an associate or joint venture that becomes a first-time adopter later than an entity that has significant influence or joint control over it.

**Parent becomes a first-time adopter later than its subsidiary**

If an entity becomes a first-time adopter later than its subsidiary (or associate or joint venture), the entity should, in its CFS, measure the assets and liabilities of the subsidiary (or associate or joint venture) at the same carrying amounts as in the financial statements of the subsidiary (or associate or joint venture), after adjusting for consolidation and equity accounting adjustments and for the effects of the business combination in which the entity acquired the subsidiary.

Unlike other exemptions, this exemption does not offer a choice between different accounting alternatives. A subsidiary, which adopts Ind AS later than its parent, can choose to prepare its first Ind AS financial statements by reference to its own date of transition to Ind AS or that of its parent. However, the parent itself must use the Ind AS measurements already used in the subsidiary’s financial statements, adjusted as appropriate for consolidation procedures and the effects of business combination in which it acquired the subsidiary. This exemption does not preclude the parent from adjusting the subsidiary’s assets and liabilities for a different accounting policy, e.g., cost or revaluation for accounting for property, plant and equipment. The exemption, however, limits the choice of exemptions (e.g., the deemed cost exemption) with respect to the accounts of the subsidiary in the transition date consolidated accounts.

**Adoption of Ind AS on different dates in separate and consolidated financial statements**

An entity may sometimes become a first-time adopter for its separate financial statements earlier or later than for its CFS. For example, such a situation may arise when an entity qualifies for the exemption from preparing CFS both under the Companies Act, 2013 and Ind AS 110. Hence, in initial years, it does not prepare CFS and prepares only separate financial statements under Ind AS. Subsequently, the entity may cease to be entitled to the exemption or may choose to prepare CFS voluntarily.

If an entity becomes a first-time adopter for its separate financial statements earlier or later than for its CFS, it should measure its assets and liabilities at the same amounts in both financial statements, except for consolidation adjustments.

As drafted, the requirement is merely that the “same” basis be used, without being explicit as to which set of financial statements should be used as the benchmark. However, it seems clear from the context that the measurement basis used in whichever set of financial statements first comply with Ind AS must also be used when Ind AS are subsequently adopted in the other set.

**Joint arrangements**

Under Indian GAAP, AS 27 Financial Reporting of Interest in Joint Ventures requires all joint ventures are classified into three types, i.e., jointly controlled assets, jointly controlled operations and jointly controlled entities. An entity’s interests in jointly controlled assets/jointly controlled operations are accounted for by recognizing its share of assets, liabilities, revenue and expenses. Investment in a jointly controlled entity is accounted for by using the proportionate consolidated method.

Ind AS 111 Joint Arrangements classifies joint arrangements into two types, i.e., joint ventures and joint operations. An entity’s interest in joint operation is accounted for by recognizing its share of assets, liabilities, revenue and expenses. Investment in a joint venture is accounted for by using equity method.

On transition to Ind AS, a first time adopter is required to reassess the classification of its joint arrangements (as either joint ventures or joint operations) on the basis of Ind AS 111 criteria. Based on classification, a first time adopter may typically have to transition from the proportionate consolidation method applied under Indian GAAP to equity method under Ind AS 111.
The following table provides a step-by-step process of transition from proportionate consolidation under the previous GAAP to the equity method under Ind AS 111 on transition to Ind AS:

<table>
<thead>
<tr>
<th>Recognize investment</th>
<th>Recognize at the date of transition to Ind AS, e.g., 1 April 2015</th>
</tr>
</thead>
<tbody>
<tr>
<td>Measure investment</td>
<td>• Aggregate the carrying amounts of the assets and liabilities that the entity had previously proportionately consolidated</td>
</tr>
<tr>
<td></td>
<td>• Include any goodwill arising upon acquisition allocated from CGUs, if necessary</td>
</tr>
<tr>
<td></td>
<td>• Disclose amounts that were aggregated into the investment cost basis</td>
</tr>
<tr>
<td></td>
<td>• Do not apply initial recognition exception under Ind AS 12</td>
</tr>
<tr>
<td>Test for impairment</td>
<td>• Test if there are impairment indicators</td>
</tr>
<tr>
<td></td>
<td>• Test for impairment under Ind AS 36 methodology if indicators exist</td>
</tr>
<tr>
<td></td>
<td>• Recognize any impairment loss in retained earnings at date of transition to Ind AS</td>
</tr>
<tr>
<td>Apply equity method</td>
<td>• Subsequently account for the investment using the equity method</td>
</tr>
</tbody>
</table>

If aggregating all previously proportionately consolidated assets and liabilities results in negative net assets, an entity should assess whether it has legal or constructive obligations in relation to the negative net assets and, if so, the entity should recognize the corresponding liability. If the entity concludes that it does not have legal or constructive obligations in relation to the negative net assets, it should not recognize the corresponding liability but it should adjust retained earnings at the date of transition to Ind AS. The entity should disclose this fact, along with its cumulative unrecognized share of losses of its joint ventures at the date of transition to Ind AS.

After initial recognition at the date of transition to Ind AS, an entity should account for its investment in the joint venture using the equity method in accordance with Ind AS 28.

### Investments in subsidiaries, jointly controlled entities and associates in separate financial statements

In the preparation of separate financial statements, Ind AS 27 Separate Financial Statements requires an entity to account for its investments in subsidiaries, jointly controlled entities and associates either:

- a) At cost, or
- b) In accordance with Ind AS 109.

If a first-time adopter measures such an investment at cost, it can measure that investment at one of the following amounts in its separate opening Ind AS balance sheet:

- Cost determined in accordance with Ind AS 27
- Deemed cost, defined as
  - Fair value determined in accordance with Ind AS 113 at the date of transition to Ind AS, or
  - Previous GAAP carrying amount at the transition date.

A first-time adopter may choose to use either of these bases to measure investment in each subsidiary, joint venture or associate where it elects to use a deemed cost.
Non-controlling interest

Ind AS 110 contains specific requirements with regard to accounting for NCI. These requirements, among others, provide that:

a) An entity attributes the profit or loss and each component of OCI to the owners of the parent and NCI, even if this results in the NCI having a deficit balance.

b) When the proportion of the equity held by NCI changes, an entity adjusts the carrying amounts of the controlling and non-controlling interests to reflect the changes in their relative interests in the subsidiary. The entity recognizes directly in equity any difference between the amount by which the NCI are adjusted and the fair value of the consideration paid or received directly in equity and attributes it to the owners of the parent. Hence, no gain or loss to be recognized in profit or loss arises in this case.

c) Ind AS 110 contains specific requirements on accounting for a loss of control over a subsidiary, and the related requirements to classify all assets and liabilities of that subsidiary as held for sale.

Ind AS 101 contains a mandatory exception which requires that a first-time adopter should apply the above three requirements prospectively from its date of transition to Ind AS. However, if a first-time adopter restates any business combination that was completed prior to its date of transition to comply with Ind AS 103, it must also apply Ind AS 110, including these requirements, from that date onwards.

Financial instruments

Ind AS accounting for financial instruments is complex and requires exercise of significant judgment/estimate. In most cases, Indian entities may not have collected necessary information to apply Ind AS accounting retrospectively. Collection of past data at the transition date also may not be practical or involve the use of hindsight which is not allowed under Ind AS 101. To address these challenges, Ind AS 101 specified voluntary exemptions and mandatory exceptions related to financial instruments accounting.

Voluntary exemption: compound financial instruments

Ind AS 32 recognizes the concept of compound financial instruments, i.e., instruments containing both liability and equity components. For example, a convertible bond contains an obligation to pay interest and principal (a liability component) and an embedded conversion option (an equity component). Ind AS 32 requires an issuer to split a compound financial instrument at inception into separate liability and equity components. The measurement of two components is determined based on circumstances existing at the date when the instrument was first issued. The fair value of the liability component, excluding the conversion option, is measured at the fair value of expected cash flows at inception and recorded as a liability. The residual amount of the issuance proceeds is recorded in equity.

A first-time adopter is required to apply Ind AS 32 retrospectively and separate all compound financial instruments into their debt and equity components. Under that general principle, if the liability component of a compound financial instrument is no longer outstanding at the date of transition, retrospective application of Ind AS 32 will result in two separate equity portions: (1) a portion recorded in retained earnings that represents cumulative interest accretion on the liability component, and (2) the equity component initially allocated at inception. Since retrospective application under this situation will not affect total amount of equity recorded for this instrument, Ind AS 101 provides an exemption whereby a first-time adopter need not identify separately the two portions of equity if liability component of the instrument is no longer outstanding at the date of transition to Ind AS.
Voluntary exemption: extinguishing financial liabilities with equity instruments

Ind AS 32 recognizes the concept of compound financial instruments, i.e., instruments containing both liability and equity components. For example, a convertible bond contains an obligation to pay interest and principal (a liability component) and an embedded conversion option (an equity component). Ind AS 32 requires an issuer to split a compound financial instrument at inception into separate liability and equity components. The measurement of two components is determined based on circumstances existing at the date when the instrument was first issued. The fair value of the liability component, excluding the conversion option, is measured at the fair value of expected cash flows at inception and recorded as a liability. The residual amount of the issuance proceeds is recorded in equity.

A first-time adopter is required to apply Ind AS 32 retrospectively and separate all compound financial instruments into their debt and equity components. Under that general principle, if the liability component of a compound financial instrument is no longer outstanding at the date of transition, retrospective application of Ind AS 32 will result in two separate equity portions: (1) a portion recorded in retained earnings that represents cumulative interest accretion on the liability component, and (2) the equity component initially allocated at inception. Since retrospective application under this situation will not affect total amount of equity recorded for this instrument, Ind AS 101 provides an exemption whereby a first-time adopter need not identify separately the two portions of equity if liability component of the instrument is no longer outstanding at the date of transition to Ind AS.

Exemptions/exceptions related to classification of financial assets

Under Ind AS 109, all financial assets are classified into three principal categories for measurement purposes. These categories are amortized cost, fair value through other comprehensive income (FVTOCI) and fair value through profit or loss (FVTPL). “Amortized cost” measurement is applicable only for “debt instruments” An entity may use FVTPL and FVTOCI categories both for debt and equity instruments. The classification depends on the following two criteria and options elected by the entity:

a) The entity’s business model for managing the financial assets, and

b) The contractual cash flow characteristics of the financial asset.

Ind AS 109 requires an entity to decide classification of financial assets on initial recognition, i.e., when it becomes party to the terms of contract. It is allowed to change such classification at a later date only in limited circumstances.

Voluntary exemptions

Considering practical difficulties in applying Ind AS 109 classification requirements retrospectively, Ind AS 101 contains the following voluntary exemptions:

a) Designation of financial asset as measured at fair value through profit or loss (FVTPL): In accordance with Ind AS 109, an entity may designate a financial asset, which is a debt instrument and otherwise meets amortized cost or FVTOCI criteria, as at FVTPL. However, such designation is allowed only if doing so reduces or eliminates a measurement or recognition inconsistency (commonly referred to as “accounting mismatch”). Ind AS 109 also requires that an entity should apply “accounting mismatch” criteria and decide whether to apply FVTPL designation on the date of initial recognition of the financial asset.

A first-time adopter is allowed to designate a financial asset as at FVTPL on the basis of facts and circumstances existing at the date of transition to Ind AS. An entity exercising this exemption needs to make certain additional disclosures, i.e., fair value of financial assets so designated at the date of designation and their classification and carrying amount in the previous financial statements.

b) Designation of investment in equity instruments: Ind AS 109 allows an entity to make an irrevocable election to designate an investment in an equity instrument not held for trading as at FVTOCI, instead of FVTPL. It requires such election to be made on initial recognition and cannot be changed subsequently. A first-time adopter is allowed to designate an investment in such an equity instrument as at FVTOCI on the basis of facts and circumstances that existed at the date of transition to Ind AS.

To illustrate, consider that an entity, on the date of its transition, is holding certain equity investments for strategic purposes. The entity can designate these equity investments as at FVTOCI, without looking at its intention on the date it acquired these investments.
Mandatory exception

Ind AS 101 also contains the following mandatory exception related to classification of financial assets.

In accordance with Ind AS 109, a financial asset which is a debt instrument is measured at amortized cost if it meets two tests, i.e., business model test and SPPI test, at the date of its initial recognition. A first-time adopter must assess whether a financial asset meets these test on the basis of facts and circumstances existing at the date of transition to Ind AS.

The SPPI test in Ind AS 109 is based on the premise that contractual cash flows give the holder a return which is in line with a “basic lending arrangement”. However, if the terms of contract contain features which may modify the time value of money, the SPPI test is not met requiring the entity to measure the entire debt instrument as at FVTPL.

To make passing of the SPPI test easier, Ind AS 109 contains certain operational simplifications. For example, Ind AS 109 states that (a) modified time value of money element and/or (b) prepayment feature in a debt instrument do not fail the SPPI test if their impact is insignificant at the time of initial recognition of the financial asset.

Ind AS 101 states that if a first-time adopter is unable to assess these particular aspects about the nature of cash flows on the basis of facts and circumstances at the time of initial recognition of the financial asset, it will lose the benefit of operational simplification designed to make passing the SPPI test easier. In other words, if these features are present in the asset and information about facts and circumstances that existed at the time of initial recognition of the financial asset is not available, the first-time adopter will assume that SPPI test has failed.

Exemptions related to classification of financial liabilities

Under Ind AS 109, financial liabilities are classified either as at FVTPL or amortized cost. Ind AS 109 requires an entity to decide classification of financial liabilities on initial recognition. No subsequent reclassification of financial liabilities is allowed.

Ind AS 101 contains the following exemptions pertaining to classification of financial liabilities:

a) Designation of financial liability at fair value through profit or loss: Ind AS 109 permits an entity to designate a financial liability as at FVTPL if the prescribed criteria are met at the time of initial recognition of the financial liability. A first-time adopter is allowed to designate a financial liability as at FVTPL provided the liability meets Ind AS 109 criteria at the date of transition to Ind AS.

b) Determination of an accounting mismatch for presenting a gain or loss on financial liability: Ind AS 109 requires that for financial liabilities designated as at FVTPL, changes in the fair value attributable to own credit risk are recognized in the OCI. However, if this requirement will create or enlarge an accounting mismatch in profit or loss, the entity should present all gains or losses on that liability (including the effects of changes in credit risk for that liability) in profit or loss. Ind AS 109 requires an entity to make accounting mismatch assessment on the date it becomes a party to the financial liability (i.e., on initial recognition). Ind AS 101 allows a first-time adopter to make this determination based on the facts and circumstances that exist at the date of transition to Ind AS.

Mandatory exception: application of effective interest rate

Ind AS 109 requires certain categories of financial assets and liabilities to be measured at amortized cost using the effective interest method. In accordance with Ind AS 109, “effective interest rate” is the rate that exactly discounts estimated future cash payments or receipts through the expected life of the financial asset or financial liability to the gross carrying amount of a financial asset or to the amortized cost of a financial liability.

Ind AS 101 typically requires a first-time adopter to apply the above requirement retrospectively, i.e., from the date of initial recognition of the financial asset/liability. However, it acknowledges that in some cases, a first time adopter may find it impractical to apply the effective interest method in Ind AS 109 retrospectively. If this is the case, the fair value of financial asset or the financial liability at the date of transition to Ind AS is the new gross carrying amount of that financial asset or the new amortized cost of that financial liability.

As stated above, Ind AS 8 lays down very strict criteria for concluding whether it is impractical to apply a requirement of Ind AS retrospectively. In accordance with Ind AS 8, applying a requirement is impracticable when the entity cannot apply it after making every reasonable effort to do so.
Voluntary exemption: fair value measurement of financial assets or liabilities at initial recognition

Ind AS 109 states that the fair value of a financial instrument on initial recognition is normally the transaction price (i.e., the fair value of the consideration given or received). However, if an entity determines that the fair value at initial recognition differs from the transaction price, Ind AS 109 contains specific requirement with regard to accounting for the differences. Specifically, Ind AS 109 requires that if the fair value is evidenced by a quoted price in an active market for an identical asset or liability (i.e., a level 1 input) or based on a valuation technique which uses only data from observable markets, the entity recognizes difference between the fair value at initial recognition and the transaction price as a gain or loss in profit or loss. In all other cases, the entity cannot recognize upfront gain/losses.

Ind AS 101 provides a transition relief from the above requirement. Consequently, a first-time adopter need not apply the requirements of Ind AS 109 (in determining whether recognition of day 1 gain/loss is appropriate) to the transactions entered into before the date of transition to Ind AS.

Voluntary exemption: designation of contracts to buy or sell a non-financial item

Ind AS 109 contains specific guidance for contracts to buy or sell a non-financial item that can be settled net in cash or another financial instrument, or by exchanging financial instruments. It requires such contracts to be accounted for as derivatives. However, Ind AS 109 scopes out contracts which are entered into and continue to be held for receipt or delivery of a non-financial item in accordance with the entity’s expected purchase, sale or usage requirements. Contracts scoped out from Ind AS 109 are treated as executory contracts under Ind AS 37 Provisions, Contingent Liabilities and Contingent Assets.

Notwithstanding the above, Ind AS 109 states that if an entity elects to designate a scoped out contract as at fair value through profit or loss (FVTPL), Ind AS 109 will apply to those contracts and they will be treated as derivative. Ind AS 109 permits FVTPL designation for the scoped out contracts only at the time of initial recognition and only if FVTPL designation eliminates or significantly reduces a recognition inconsistency (accounting mismatch) that would otherwise arise.

For contracts that were previously entered into and are outstanding at the date of transition to Ind AS, Ind AS 101 gives a voluntary exemption whereby a first-time adopter can make FVTPL designation as at the date of its transition to Ind AS. However, such designation is allowed only if the contracts meet the requirements of Ind AS 109 at that date and the entity designates all similar contracts.

Mandatory exception: impairment of financial assets

Ind AS 109 introduces a new “expected credit loss model” for impairment of financial assets. Ind AS 101 requires a first-time adopter to apply impairment requirements of Ind AS 109 retrospectively. However, it gives certain operational simplifications in applying these requirements. On transition to Ind AS, a first time adopter is required to approximate the credit risk on initial recognition of the financial instrument (or, for loan commitments and financial guarantee contracts, the date that the entity became a party to the irrevocable commitment), by considering all reasonable and supportable information that is available without undue cost or effort. The entity will compare credit risk so identified on initial recognition to the credit risk at the date of transition to Ind AS for determining whether 12-month ECL or lifetime ECL should be used.

If, at the date of transition to Ind AS, an entity is unable to determine whether there have been significant increases in credit risk since initial recognition without undue cost or effort, then the entity must recognize a loss allowance based on lifetime ECL at each reporting date until the financial instrument is derecognized.

Mandatory exception: derecognition of financial assets and liabilities

Ind AS 109 deals with derecognition of financial assets and financial liabilities in a comprehensive manner. Ind AS 109 derecognition rules for financial assets are extremely complex. The decision whether a transfer qualifies for derecognition is made by applying a combination of risk and rewards and control tests. The use of two models often create confusion however, those have been addressed by ensuring that the risk and rewards test is applied first, with the control test used only when the entity has neither transferred substantially all risks and rewards of the asset nor retained them. Derecognition cannot be achieved by only a legal transfer. The transfer has to happen in substance which is evaluated by using a risk and rewards and a control model. A legal opinion from a qualified attorney is normally required to conclude on highly complex matters.
Due to the application of Ind AS 109 derecognition requirements, an entity may not be able to derecognize financial assets transferred under the arrangements, such as, bill discounting and/or factoring of trade receivables, in entirety, if it has provided credit enhancement to the transferor. Rather, based on the specific facts, the entity will evaluate whether it should treat the transfer as a financing transaction (i.e., debt) or continuing involvement approach will apply which requires the entity to continue recognizing the transferred asset to the extent of its continuing involvement.

A first-time adopter may not have collected the requisite information to apply Ind AS 109 requirement to transfer of financial assets/liabilities which has taken place before the transition date. Ind AS 101 requires a first-time adopter to apply derecognition requirements in Ind AS 109 prospectively to transactions occurring on or after the date of transition to Ind AS. For example, if a first-time adopter derecognized non-derivative financial assets or non-derivative financial liabilities under its previous GAAP as a result of a transaction that occurred before the date of transition to Ind AS, the entity does not recognize those assets or liabilities under Ind AS unless they qualify for recognition as a result of a later transaction or event. However, a first-time adopter may apply derecognition requirements retrospectively from a date of the entity's choosing provided that the information needed to apply Ind AS 109 to financial assets and financial liabilities derecognized as a result of past transactions was obtained at the time of initially accounting for those transactions. This is likely to prevent many first-time adopters from restating transactions that occurred before the date of transition to Ind AS.

Mandatory exception: embedded derivatives

Ind AS 109 does not permit embedded derivatives to be separated from host contracts that are financial assets. Rather, an entity applies Ind AS 109 classification requirements to the entire hybrid contract. In case of all other contracts, Ind AS 109 requires that an embedded derivative should be separated from the host contract and accounted for as a derivative if, and only if:

a) The economic characteristics and risks of the embedded derivative are not closely related to the economic characteristics and risks of the host contract,

b) A separate instrument with the same terms as the embedded derivative would meet the definition of a derivative, and

c) The hybrid (combined) instrument is not measured at fair value with changes in fair value recognized in the statement of profit and loss (i.e., a derivative that is embedded in a financial liability at fair value through profit or loss is not separated).

Ind AS 101 requires a first-time adopter to assess whether an embedded derivative should be separated from the host contract and accounted for as a derivative based on conditions that existed at the later of the date it first became a party to the contract and the date a reassessment is required by Ind AS 109. Ind AS 109 requires subsequent reassessment of embedded derivatives only if there is a change in the terms of the contract that significantly modifies the cash flows that otherwise would be required under the contract. Hence, unless there is any such modification in the contract, a first-time adopter needs to make embedded derivative assessment based on conditions existing on the date it first became a party to the contract.

Mandatory exception: hedge accounting

Under Indian GAAP, there is no mandatory standard that deals comprehensively with derivative and hedge accounting. The ICAI has recently issue the Guidance Note on Accounting for Derivative Contracts. The said Guidance Note will be applicable from financial year beginning on or after 1 April 2016. The absence of comprehensive guidance on hedge accounting has resulted in the adoption of varying practices.

a) Loss on derivative contracts is recognized; while the gain, if any, is ignored. For this purpose, an entity may compute gain/loss on an individual instrument basis or on a portfolio basis.

b) Gain/loss on derivative contract is offset against the loss/gain on the underlying hedged item and net loss, if any, is recognized in P&L. For example, entities may recognize net loss on forward exchange contracts after offsetting gain on the hedged highly probable forecast sale transaction.

c) Accounting for derivative contracts is subsumed in accounting for the underlying hedged item. For example, entities may treat floating rate loan and interest rate swap entered to hedge the cash flow risk of the loan together and, therefore, recognize interest on the loan at fixed rate. Any further gain/loss on the swap are not recognized.
d) Some entities have applied hedge accounting principles of AS 30 *Financial Instruments: Recognition and Measurement*, without adopting AS 30 in entirety. For instance, entities may recognize gains/losses on derivative instruments undertaken to hedge cash flow risk in a hedging reserve account, without complying with strict hedge documentation requirements.

In accordance with Ind AS 109, all derivatives are measured at fair value, and any gains/losses, except those on derivatives used for hedge purposes, are recognized in profit or loss. Ind AS 109 deals with hedge accounting in a comprehensive manner. It defines three types of hedging relationships, namely, fair value hedges, cash flow hedges and hedges of net investments in a foreign operation. It also lays down prerequisite conditions to apply hedge accounting.
Ind AS 101 requires that a first time adopter should measure all derivatives at fair value on transition to Ind AS. Moreover, the entity is required to eliminate deferred gains and losses arising on derivatives that were reported in accordance with previous GAAP as if they were assets or liabilities. The recognition of resulting gain/loss is determined in accordance with the mandatory exception laid down in Ind AS 101. The flowchart presentation of the exception is as follows:

**Hedge relationship which still exists was designated under previous GAAP before date of transition to Ind AS?**

- **Yes**
  - **On transition**
    - **Fair value hedge**
    - **Cash flow hedge**
      If hedging instrument is no longer outstanding, there is no requirement to restate when under previous GAAP its result has been recognized in P&L and not deferred.
  - **After transition**
    - Are the CONDITIONS for hedge accounting in Ind AS 109 met?
      - **Yes**
        - Follow specific hedge accounting guidance in Ind AS 109
      - **No**
        - Apply Ind AS 109 to prospectively discontinue hedge accounting

- **No**
  - **Hedge is not reflected in the opening Ind AS balance sheet.**

**Did the entity designate a net position as a hedged item in accordance with previous GAAP?**

- **Yes**
  - Entity may designate on or before the date of transition to Ind AS an individual item within the net position as a hedged item or a net position that meets requirements in Ind AS 109
    - Follow specific guidance for cash flow or fair value hedges on transition and subsequently

- **No**
  - **Hedge is not reflected in the opening Ind AS balance sheet.**

The application of the hedge accounting exception in some typical Indian scenarios is explained below with the help of simple examples. These scenarios do not consider the impact of the Guidance Note on Accounting for Derivative Contracts since it is not mandatory yet.
Example 7: Cash flow hedge of highly probable foreign currency sale

FTA Limited expects to make foreign currency sale of US$3,000,000 on 31 December 2015. The functional currency of FTA is INR. On 1 January 2014, FTA determines that sale is highly probable and it enters into a forward contract to hedge the foreign currency risk. According to the terms of the forward contract, FTA will pay US$3,000,000 on 31 December 2015 and receive INR @ INR 65 per US$. FTA’s date of transition to Ind AS is 1 April 2015.

How should FTA treat derivative contract in its Ind AS opening balance sheet? Consider the following scenarios:

(i) FTA recognizes mark-to-market loss on derivative in its profit or loss, without considering offsetting gain on the hedged item. At the transition date, there is a cumulative gain on the hedged item, which is not recognized on consideration of prudence.

(ii) FTA recognizes mark-to-market gain/loss on the forward contract in the Cash Flow Hedge Reserve. However, it has not maintained detailed hedge documentation.

(iii) FTA has identified hedge relationship under Indian GAAP and it does not recognize gain/loss on the forward contract since the same will be offset by loss/gain on the hedged item. At the date of transition to Ind AS, the hedged item is still expected to occur.

(iv) FTA has identified hedge relationship under Indian GAAP and it does not recognize gain/loss on the forward contract since the same will be offset by loss/gain on the hedged item. At the transition date, the hedged item is not expected to occur.

In the first scenario, FTA has not identified hedge relationship under Indian GAAP. On the transition date, it will measure the forward contract at its fair value and recognize resulting gain in the opening retained earnings. Hence, there is no change in Indian GAAP accounting going forward also, except that FTA will also start recognizing gains immediately.

In the second scenario, though FTA has not maintained detailed hedge documentation, it has identified hedge relationship under Indian GAAP. Moreover, the relationship is an eligible hedge relationship under Ind AS 109. Hence, in its opening Ind AS balance sheet, FTA will recognize gain/loss on the forward contract, arising before the date of transition to Ind AS, in the Cash Flow Hedge Reserve. FTA will reclassify this amount to P&L when the hedged item (i.e., foreign currency sale) impacts the profit or loss. Ind AS 101 is clear that after the date of transition to Ind AS, hedge accounting can be applied prospectively only from the date the hedge relationship is fully designated and documented in accordance with Ind AS 109 requirements. Hence, if FTA wishes to continue applying hedge accounting after the date of transition to Ind AS, it must complete designation and documentation of the hedge relationship on or before that date. FTA must also comply with ongoing requirements related to hedge effectiveness, etc. If FTA does not comply with hedge accounting requirements of Ind AS 109, it will compute fair value of the derivative contract at each reporting date and recognize gain/loss in profit or loss immediately. However, the gain or loss in the cash flow hedge reserve as of the date of transition will continue to be shown there and can be reclassified to P&L only when the hedged transaction occurs.

In third scenario, the same analysis as the second scenario applies both regard to accounting at the transition date as well as accounting after the transition date. Consequently, FTA will recognize gain/- loss on the forward contract, arising on or before the transition date, in the Cash Flow Hedge Reserve in its opening Ind AS balance sheet. Like the second scenario, subsequent accounting also depends on whether FTA complies with Ind AS 109 hedge requirements.

In the fourth scenario, the hedged item is no longer expected to occur. Hence, it is a relationship of the type that does not qualify for hedge accounting under Ind AS 109. Consequently, FTA should not reflect this hedging relationship in its opening Ind AS balance sheet. Rather, FTA will recognize fair value gain/loss arising on the forward contract in the opening retained earnings. Going forward, assume that FTA does not comply with hedge accounting requirements of Ind AS 109. Hence, FTA will fair value the derivative contract at each reporting date and recognize gain/loss in profit or loss immediately.
Example 8: Cash flow hedge of interest rate risk

In 2009, FTA Limited borrowed US$10 million from a bank. The terms of the loan provide that a coupon of 3 month LIBOR plus 2% is payable quarterly in arrears and the principal is repayable in 2024. In 2012, FTA decided to “fix” its coupon payments for the remainder of the term of the loan by entering into a twelve-year pay-fixed, receive-floating interest rate swap. The swap has a notional amount of US$10 million and the floating leg resets quarterly based on 3 month LIBOR.

In FTA’s last financial statements prepared under Indian GAAP, the swap was clearly identified as a hedging instrument in a hedge of the loan and was accounted for as such. The fair value of the swap was not recognized in the balance sheet and periodic interest settlements were accrued and recognized as an adjustment to the loan interest expense. On 1 April 2015, FTA’s date of transition to Ind AS, the loan and the swap were still in place and the swap had a positive fair value of US$1 million and a nil carrying amount. In addition, FTA met all the conditions in Ind AS 109 to permit the use of hedge accounting for this arrangement throughout years ended 31 March 2016 and 2017.

In its opening Ind AS balance sheet, FTA should:

- Recognize the interest rate swap as an asset at its fair value of USD 1 million, and
- Credit US$1 million to the Cash Flow Hedge Reserve, to be reclassified to profit or loss as the hedged transactions (future interest payments on the loan) affect profit or loss.

In addition, hedge accounting will be applied throughout the years ended 31 March 2016 and 2017.

Example 9: Fair value hedge of inventory

On 15 November 2014, FTA Limited entered into a forward contract to sell 50,000 barrels of crude oil to hedge all changes in the fair value of certain inventory. FTA will apply Ind AS 109 from 1 April 2015, its date of transition to Ind AS. The historical cost of the forward contract is nil and at the date of transition the forward contract had a negative fair value of US$50.

In FTA’s final financial statements prepared under Indian GAAP, the forward contract was clearly identified as a hedging instrument as a hedge of the inventory. FTA has not recognized the forward contract liability in its Indian GAAP balance sheet since the loss was offset by a corresponding gain on the inventory. Due to the requirements of AS 2 Valuation of Inventories, FTA has also not recognized unrealized gain on inventory in its Indian GAAP balance sheet. FTA met all the conditions in Ind AS 109 to permit the use of hedge accounting for this arrangement until the forward expired.

In its opening Ind AS balance sheet, FTA should:

- Recognize the forward contract as a liability at its fair value of US$50,
- Recognize the crude oil inventory at its historical cost plus lower of the change in fair value of the crude oil inventory and that of the forward contract, and
- Record the net adjustment in the opening retained earnings.

In addition, hedge accounting will be applied until the forward expired.
Mandatory exception: government loans

In many developing countries, the government provides interest free loan or loans carrying interest at below market rate to entities so as to promote economic development. For example, in India, many state governments provide sales tax deferral scheme to encourage and ensure development of underdeveloped areas.

Under Indian GAAP, AS 12 Accounting for Government Grants does not specifically deal with accounting for government loan at nil or below-market rate of interest. However, AS 29 Provisions, Contingent Liabilities and Contingent Assets prohibits discounting of sales tax deferral or any other concessional loan given by the government. Hence, under Indian GAAP, government loans at nil or concessional rate are recognized at nominal value.

Ind AS 20 Accounting for Government Grants and Disclosure of Government Assistance requires the benefit of a government loan at nil or below-market rate of interest to be treated as a government grant. On initial recognition, the loan is measured at its fair value determined in accordance with Ind AS 109. The difference between the initial fair value of the loan and the proceeds received is a government grant to be recognized in accordance with Ind AS 20. Going forward, the loan is measured at amortized cost using the effective interest method.

Ind AS 101 contains a mandatory exception with regard to government loans. In accordance with the exception, a first-time adopter should classify government loan received as a financial liability or an equity instrument in accordance with the principles of Ind AS 32. A first-time adopter will apply the requirements in Ind AS 109 prospectively to government loans existing at the date of transition to Ind AS. Hence, a first-time adopter will not recognize the corresponding benefit of the government loan at a below-market rate of interest as a government grant. If a first-time adopter, under its previous GAAP, did not recognize and measure a government loan at a below-market rate of interest on a basis consistent with Ind AS requirements, it needs to use its previous GAAP carrying amount of the loan at the date of transition as the carrying amount of the loan in the opening Ind AS balance sheet. It will apply Ind AS 109 to the measurement of such loans after the date of transition to Ind AS. To do so, the entity calculates the effective interest rate by comparing the carrying amount of the loan at the date of transition to Ind AS with the amount and timing of expected repayments to the government. If the loan is repayable at the carrying amount appearing in the opening Ind AS balance sheet, no interest will be recognized on the loan.

Example 10: Government loan with below-market interest rate

FTA Limited’s date of transition to Ind AS is 1 April 2015. In 2011, FTA had received a loan of INR1 million at a below-market rate of interest from the government. Under its previous GAAP, FTA accounted for the loan as a liability without discounting the same and its carrying amount at the transition date was INR1 million. The amount repayable at 1 April 2018 is INR1 million.

No other payment is required under the terms of the loan and there are no future performance conditions attached to it. The information needed to measure the fair value of the loan was not obtained at the time it was initially accounted for.

The loan meets the definition of a financial liability in accordance with Ind AS 32. FTA therefore continues to classify it as a liability. It also uses the previous GAAP carrying amount of the loan at the date of transition as the carrying amount of the loan in the opening Ind AS balance sheet. Since the loan does not carry any interest and is repayable at the amount recognized in the opening balance sheet, interest does not need to be recognized on the loan.
Other miscellaneous exemptions and exceptions

Mandatory exception

Estimates

In preparing the opening Ind AS balance sheet and comparative information in its first Ind AS financial statements, a first-time adopter may have received new information about estimates that it made for the same dates under previous GAAP. Ind AS contains a mandatory exception which will not allow the use of such new/additional information to change the previous GAAP estimates. Ind AS 101 requires an entity to use estimates under Ind AS that are consistent with the estimates made for the same date under its previous GAAP - after adjusting for any difference in accounting policy - unless there is objective evidence that those estimates were in error.

Under Ind AS 101, an entity cannot apply hindsight and make “better” estimates when it prepares its first Ind AS financial statements. This also means that an entity is not allowed to consider subsequent events that provide evidence of conditions that existed at that date, but that came to light after the date its previous GAAP financial statements were finalized.

An entity may receive information after the date of transition to Ind AS about estimates that it had made under previous GAAP. The entity should treat the receipt of such information as non-adjusting event, in accordance with Ind AS 10 Events after the Reporting Period. For example, assume that an entity’s date of transition to Ind AS is 1 April 2015 and new information on 15 July 2015 requires the revision of an estimate made in accordance with previous GAAP as at 31 March 2015. The entity should not reflect that new information in its opening Ind AS Balance Sheet (unless the estimates need adjustment for any differences in accounting policies or there is objective evidence that the estimates were in error). Instead, the entity should reflect that new information in profit or loss (or, if appropriate, other comprehensive income) for the year ended 31 March 2016.

When an entity needs to make estimates under Ind AS at the date of transition to Ind AS that were not required under its previous GAAP, those estimates should be consistent with Ind AS 10 and reflect conditions that existed at the date of transition to Ind AS. This means, for example, that estimates of market prices, interest rates or foreign exchange rates should reflect market conditions at the date of transition to Ind AS.

The following chart summarizes Ind AS 101 requirements relating to estimates:

```
<table>
<thead>
<tr>
<th>Did the entity make estimate under its previous GAAP?</th>
</tr>
</thead>
<tbody>
<tr>
<td>Yes</td>
</tr>
<tr>
<td>No</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Is there objective evidence that the estimate was an error?</th>
</tr>
</thead>
<tbody>
<tr>
<td>Yes</td>
</tr>
<tr>
<td>No</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Did the entity use accounting policy consistent with Ind-AS?</th>
</tr>
</thead>
<tbody>
<tr>
<td>Yes</td>
</tr>
<tr>
<td>No</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Make estimate reflecting conditions at the relevant date*</th>
</tr>
</thead>
<tbody>
<tr>
<td>Use previous GAAP estimate</td>
</tr>
</tbody>
</table>

Adjust previous estimate to reflect differences in accounting policies

*The relevant date is the date to which the estimate relates.
The above provisions also apply to a comparative period presented in an entity’s first Ind AS financial statements, in which case the references to the date of transition to Ind AS are replaced by references to the end of that comparative period.

Example 11: Application of Ind AS 101 to estimates

Background

FTA Limited accounted for inventories at the lower of cost and net realizable value under Indian GAAP. Entity A’s accounting policy is consistent with the requirements of Ind AS 2 Inventories. Under Indian GAAP, the goods were accounted for at a price of INR 1.25 per kg. Due to changes in market circumstances, FTA ultimately could only sell the goods in the following period for INR 0.90 per kg.

Application of the requirements

Assuming that FTA’s estimate of the net realizable value was not in error, it will account for the goods at INR 1.25 per kg upon transition to Ind AS and will make no adjustments because the estimate was not in error and its accounting policy was consistent with Ind AS. The effect of selling the goods for INR 0.90 per kg will be reflected in the period in which they were sold.
Voluntary exemptions

Share-based payments

Under Indian GAAP, the Guidance Note on Accounting For Employee Share-based Payments permits an entity to use the intrinsic value method as an alternate to the fair value method for measuring an employee share-based payment. On transition to Ind AS, all entities need to measure share-based payment transactions using the fair value method only.

Under Ind AS 101, there is no exemption from recognizing share-based payment transactions that have not yet vested at the date of transition to Ind AS. The voluntary exemptions in Ind AS 101 clarify that a first-time adopter is encouraged, but not required, to apply Ind AS 102 to equity instruments that vested before date of transition to Ind AS. However, if a first-time adopter elects to apply Ind AS 102 to such equity instruments, it may do so only if the entity has disclosed publicly the fair value of those equity instruments, determined at the measurement date, as defined in Ind AS 102.

Ind AS 101 requires that for all grants of equity instruments to which Ind AS 102 has not been applied (e.g., equity instruments vested but not settled before date of transition to Ind AS), a first-time adopter must still make the principal disclosures relating to the nature and extent of share-based payments required by paragraphs 44 and 45 of Ind AS 102.

If a first-time adopter modifies the terms or conditions of a grant of equity instruments to which Ind AS 102 has not been applied, the entity is not required to apply paragraphs 26–29 of Ind AS 102 if the modification occurred before the date of transition to Ind AS.

A first-time adopter is encouraged, but not required, to apply Ind AS 102 to liabilities arising from share-based payment transactions that were settled before the date of transition to Ind AS.

Long-term foreign currency monetary items

Under Indian GAAP, AS 11 The Effects of Changes in Foreign Exchange Rates gives two options with regard to accounting for exchange differences. The first option is that an entity recognizes exchange differences as income or expense in profit or loss in the period in which they arise. However, AS 11 provides companies an option to defer/capitalize exchange differences arising on long-term foreign currency monetary items. The option once selected is irrevocable and needs to be applied to all long-term foreign currency monetary items. A long-term foreign currency monetary item is an item with a term of 12 months or more at the date of its origination.

Ind AS 21 The Effects of Changes in Foreign Exchange Rates requires exchange differences arising on translation/settlement of all foreign monetary items, including long-term foreign currency monetary items, to be recognized as income or expense in profit or loss in the period in which they arise. Ind AS 21 does not give any deferral/capitalization option.

Notwithstanding the above, Ind AS 101 contains a voluntary exemption whereby companies which have adopted deferral/capitalization accounting under AS 11 can continue to use deferral/amortization policy for exchange differences arising on translation of long-term foreign currency monetary items recognized in the financial statements for the period ending immediately before the beginning of the first Ind AS financial reporting period. It should be noted that this is an option. In other words, a company is free to use Ind AS 21 accounting even for exchange differences arising on translation of long-term foreign currency monetary items recognized in financial statements for the period ending immediately before the beginning of the first Ind AS financial reporting period.

Consider that a company will apply Ind AS for the first time in its financial statements for the year ended 31 March 2017. Its date of transition is 1 April 2015 and its last Indian GAAP financial statements were prepared for the year ended 31 March 2016. For any long-term foreign currency monetary items recognized on or before 31 March 2016, the company has option of continuing deferral/amortization of exchange differences. For any long-term foreign currency monetary item recognized on or after 1 April 2016, deferral/amortization of exchange difference will not be allowed. Rather, the company will apply Ind AS 21 for recognition of gains and losses.

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4 Please also refer the booklet titled “IFRS-converged Indian Accounting Standards - Outreach meeting dated 15 January 2015”, published by the Accounting Standards Board of the ICAI.
This exemption does not exist under IASB IFRS. Hence, if an entity decides to use this exemption, it will depart from IASB IFRS.

**Stripping costs in the production phase of a surface mine**

In surface mining operations, entities may find it necessary to remove mine waste materials ("overburden") to gain access to mineral ore deposits. This waste removal activity is known as "stripping". A mining entity may continue to remove overburden and to incur stripping costs during the production phase of the mine. Appendix B to Ind AS 16 *Stripping Costs in the Production Phase of a Surface Mine* considers when and how to account separately for the benefits arising from a surface mine stripping activity, as well as how to measure these benefits both on initial recognition and subsequently.

A first-time adopter may apply the Appendix B to Ind AS 16 from the date of transition to Ind AS. As at transition date to Ind AS, any previously recognized asset balance that resulted from stripping activity undertaken during the production phase ("predecessor stripping asset") is reclassified as part of an existing asset to which the predecessor stripping asset can be associated. Such balances are depreciated or amortized over the remaining expected useful life of the identified component of the ore body to which each predecessor stripping asset balance relates. If there is no identifiable component of the ore body to which that predecessor stripping asset relates, it should be recognized in the opening retained earnings at the transition date to Ind AS.

**Non-current assets held for sale and discontinued operations**

Ind AS 105 *Non-current Assets Held for Sale and Discontinued Operations* requires that non-current assets (or disposal groups) that meet criteria to be classified as held for sale or for distribution should be carried at the lower of its carrying amount and fair value less cost to sell on the initial date of such identification. Ind AS 105 also requires that a non-current asset classified as held for sale or forming part of disposal group should not be depreciated, if its measurement is covered within the scope of Ind AS 105.

Ind AS 101 contains a voluntary exemption whereby a first time adopter can:

- Measure such assets or operations at the lower of carrying value and fair value less cost to sell at the date of transition to Ind AS in accordance with Ind AS 105, and
- Recognize directly in retained earnings any difference between that amount and the carrying amount of those assets at the date of transition to Ind AS determined under the entity's previous GAAP.

One of the consequences of this exemption is that the first time adopter will not be required to reverse depreciation/amortization charged under the previous GAAP on non-current assets, which meets the criteria for classification as held for sale on the date of transition to Ind AS.

This exemption does not exist under IASB IFRS. Hence, if an entity decides to use this exemption, it will depart from IASB IFRS.

**Deemed cost for oil and gas assets**

It is common practice under some country GAAPs, including Indian GAAP, to measure Exploration &Evaluation assets, using the "full cost accounting" method. However, this method is not consistent with Ind AS. Applying Ind AS retrospectively would pose significant problems for first-time adopters because it will also require amortization to be calculated (on a unit of production basis) for each year, using a reserves base that has changed over time because of changes in factors such as geological understanding and prices for oil and gas. In many cases, this information may not be available.

Ind AS 101 therefore grants voluntary exemption for first time adopters. A first-time adopter using such accounting under previous GAAP may elect to measure oil and gas assets at the date of transition to Ind AS on the following basis:

- Exploration and evaluation assets at the amount determined under the entity's previous GAAP, and
- Assets in the development or production phases at the amount determined for the cost center under the entity's previous GAAP. The entity should allocate this amount to the cost center's underlying assets pro rata using reserve volumes or reserve values as of that date.
To avoid the use of deemed costs resulting in an oil and gas asset being measured at more than its recoverable amount, the entity should test exploration and evaluation assets and assets in the development and production phases for impairment at the date of transition to Ind AS. The deemed cost amounts should be reduced to take account of any impairment charge, if any.

**Deemed cost for assets used in operations subject to rate regulation**

Some entities hold items of property, plant and equipment or intangible assets that are used, or were previously used, in operations subject to rate regulation. The carrying amount of such items may include amounts that were determined under previous GAAP but do not qualify for capitalization in accordance with Ind AS. If this is the case, a first-time adopter may elect to use the previous GAAP carrying amount of such an item at the date of transition to Ind ASs as deemed cost.

If an entity applies this exemption to an item, it need not apply it to all items. At the date of transition to Ind AS, an entity should test for impairment in accordance with Ind AS 36 each item for which this exemption is used.

**Presentation and disclosures**

An entity’s first Ind AS financial statements should include at least three balance sheets, two statements of profit and loss, two statements of cash flows and two statements of changes in equity and related notes.

The first Ind AS financial statements should be presented in accordance with the presentation and disclosure requirements in Ind AS 1 Presentation of Financial Statements and other Ind AS standards. In addition, the presentation and disclosures in the financial statements should also comply with Schedule III of the Companies Act, 2013. Ind AS 101 does not provide exemptions from presentation and disclosure requirements in other Ind AS.

**Explanation of transition to Ind AS**

A first-time adopter should explain how the transition from Indian GAAP to Ind AS affected its reported financial position, financial performance and cash flows. These disclosures are required because they help users understand the effect and implications of the transition to Ind AS and how they need to change their analytical models to make the best use of information presented using Ind AS.

To comply with the above requirement, a first-time adopter is required to present:

- Reconciliations of its equity reported under the previous GAAP to its equity under Ind AS at:
  - The date of transition to Ind AS, and
  - The end of the latest period presented in the entity’s most recent annual financial statements under the previous GAAP.

- A reconciliation to its total comprehensive income under Ind AS for the latest period in the entity’s most recent annual financial statements. The starting point for that reconciliation should be total comprehensive income under the previous GAAP for the same period, or if an entity did not report such a total, profit or loss under the previous GAAP.
Reconciliations to be presented in first Ind AS financial statements

FTA Limited's date of transition to Ind AS is 1 April 2015 and its reporting date is 31 March 2017. It should present the primary financial statements and reconciliations in its first Ind AS financial statements.

<table>
<thead>
<tr>
<th></th>
<th>1 April 2015</th>
<th>31 March 2016</th>
<th>31 March 2017</th>
</tr>
</thead>
<tbody>
<tr>
<td>Balance sheet under Ind AS</td>
<td>Yes</td>
<td>Yes</td>
<td>Yes</td>
</tr>
<tr>
<td>Reconciliation of equity to Indian GAAP</td>
<td>Yes</td>
<td>Yes</td>
<td>No</td>
</tr>
<tr>
<td>For the period ending under Ind AS</td>
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<tr>
<td>Statement of total comprehensive income</td>
<td>NA</td>
<td>Yes</td>
<td>Yes</td>
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<tr>
<td>Cash flow statement</td>
<td>NA</td>
<td>Yes</td>
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<td>Statement of changes in equity</td>
<td>NA</td>
<td>Yes</td>
<td>Yes</td>
</tr>
<tr>
<td>Reconciliation of total comprehensive income to Indian GAAP</td>
<td>NA</td>
<td>Yes</td>
<td>No</td>
</tr>
<tr>
<td>Explanation of material adjustments to cash flow statement prepared under Indian GAAP</td>
<td>NA</td>
<td>Yes</td>
<td>No</td>
</tr>
</tbody>
</table>

- An explanation of the material adjustments to the cash flow statement, if it presented one under its previous GAAP.
- An explanation of the material adjustments to the cash flow statement, if it presented one under its previous GAAP.

The reconciliations should give sufficient detail to enable users to understand material adjustments to the balance sheet and statement of comprehensive income. If an entity becomes aware of errors made under the previous GAAP, the reconciliations should distinguish the correction of those errors from changes in accounting policies.

These reconciliations are illustrated in Appendix 1 to this guide.

Other disclosures

If applicable, the first Ind AS financial statements should also disclose:

- If a first-time adopter has recognized or reversed any impairment losses in preparing its opening Ind AS balance sheet, the entity's first Ind AS financial statements should make disclosures that Ind AS 36 *Impairment of Assets* would have required if the entity had recognized those impairment losses or reversals in the period beginning with the date of transition to Ind AS.

- If fair value is used as deemed cost for property, plant and equipment or intangible assets or investment property, the aggregate fair values and the aggregate adjustment to the previous carrying amounts should be disclosed for each line item.

- A first time adopter to Ind AS may elect to continue with the carrying value for all of its PPE/intangible assets/investment property as recognized in financial statements as at the date of transition to Ind AS, measured according to the previous GAAP and use that as its deemed cost as the date of transition after making necessary adjustments with respect to decommissioning liabilities. If this election is made, the fact and the accounting policy should be disclosed by the entity until such time that those items of PPE, investment properties or intangible assets, as the case may be, are significantly depreciated, impaired or derecognized from the entity's balance sheet.

- An entity that applies the optional exemption to classify a financial asset or financial liability as at fair value through profit or loss must disclose:
  - The fair value of the item,
  - The carrying amount under the previous GAAP, and
  - The classification under the previous GAAP.

- If an entity uses a deemed cost in its opening Ind AS balance sheet for an investment in a subsidiary, joint venture or associate in its separate financial statements, the entity's first Ind AS separate financial statements should disclose:
  - The aggregate deemed cost of those investments for which deemed cost is their previous GAAP carrying amount
  - The aggregate deemed cost of those investments for which deemed cost is fair value, and
The aggregate adjustment to the carrying amounts reported under previous GAAP.

If an entity uses the exemption for oil and gas assets, it should disclose that fact and the basis on which carrying amounts determined under previous GAAP were allocated.

If an entity uses the exemption for operations subject to rate regulation, it should disclose that fact and the basis on which carrying amounts were determined under previous GAAP.

If an entity elects to measure assets and liabilities at fair value and to use that fair value as the deemed cost in its opening Ind AS balance sheet because of severe hyperinflation, the entity’s first Ind AS financial statements should disclose an explanation of how, and why, the entity had, and then ceased to have, a functional currency that has both of the following characteristics – a reliable general price index is not available to all entities with transactions and balances in the currency – and exchangeability between the currency and a relatively stable foreign currency does not exist.

Non-Ind AS comparative information and historical summaries

Normally Ind AS requires comparative information that is prepared on the same basis as information relating to the current reporting period. However, if an entity presents historical summaries of selected data for periods before the first period for which they present full comparative information under Ind AS, the standard does not require such summaries to comply with the recognition and measurement requirements of Ind AS.

Furthermore, some entities present comparative information in accordance with previous GAAP as well as the comparative information required by Ind AS 1. In any financial statements containing historical summaries or comparative information in accordance with previous GAAP, an entity should:

a) Label the previous GAAP information prominently as not being prepared in accordance with Ind AS; and

b) Disclose the nature of the main adjustments that would make it comply with Ind AS. An entity need not quantify those adjustments.

Interim financial reports

An entity that presents its first Ind AS financial statements is a first-time adopter and should apply Ind AS 101 in the preparation of those financial statements. It should also apply Ind AS 101 in each interim report prepared under Ind AS 34 Interim Financial Reporting for part of a period covered by its first Ind AS financial statements. For a company with a 31 March year end, this will mean that if Ind AS 34 is adopted for quarterly reporting, the first financial information prepared under Ind AS will be at 30 June 2016 and the company will need to apply Ind AS 101 in the preparation of that quarterly report. Moreover, comparable quarter, i.e., 30 June 2015 numbers will also have to be Ind AS compliant.

If a first-time adopter presents an interim financial report under Ind AS 34 for part of the period covered by its first Ind AS financial statements, then the report should include:

- A reconciliation of its equity under the previous GAAP at the end of that comparable interim period to its equity under Ind AS at that date

- A reconciliation with its total comprehensive income under Ind AS for that comparable interim period (current and year-to-date). The starting point for that reconciliation shall be total comprehensive income under the previous GAAP for that period or, if an entity did not report such a total, profit or loss under the previous GAAP.

- Reconciliations described in section “Explanation of transition to Ind AS” above or a cross-reference to another published document that includes these reconciliations.

Quarterly financial information in case of listed companies

Preparation or presentation of interim financial information for listed companies is governed by the Clause 41 of the Listing Agreement. Clause 41 currently requires that quarterly and year-to-date results should be prepared in accordance with the recognition and measurement principles laid down in AS 25 Interim Financial Reporting notified under the Company (Accounting Standards) Rules, 2006 (as amended). Once a company starts using Ind AS for annual financial statements, it will be expected that the company uses the same standards for quarterly reporting also. To address this aspect, appropriate changes need to be made in the Listing Agreement. Moreover, the listing agreement should prescribe a new format for publishing Ind AS quarterly results.
In addition to presentation of interim financial information on an ongoing basis, a specific issue needs to be considered for presentation of interim financial information in the first year of Ind AS adoption. Interim financial information provides an update to the last presented annual financial statements and should be read along with the last annual financial statements. Companies are required to prepare such information using standards that are expected to be reflected in their next annual financial statements. Considering this and the fact that Ind AS are applicable from beginning of the financial year, a company needs to start presenting Ind AS financial information from the first quarter of financial year in which it adopts Ind AS. Since the company has prepared last annual financial statements according to Indian GAAP and interim financial information is prepared using Ind AS, this may not provide meaningful update to the users. In many cases, the numbers may appear to be confusing. This issue needs to be addressed appropriately. For example, globally, in such scenarios, first-time adopters are expected to include significantly more information than would normally be included in an interim report. Examples of additional annual disclosures to be included in the entity’s first interim report could include disclosures relating to retirement benefits, income taxes, goodwill and provisions, amongst other items that significantly differ from previous GAAP and those required Ind AS disclosures that are more substantial than previous GAAP.
Ind AS conversion challenges and perspectives

Conversion to Ind AS is not just an accounting change. Rather, Ind AS implementation effort is likely to impact functions outside of the finance department, including IT, legal, sales, marketing, human resources, investor relations and senior management. In the section titled “Key differences between Ind AS and Indian GAAP”, we have explained key financial reporting impacts of transition to Ind AS. In this part, we will cover the following:

1. Direct tax impact
2. Indirect taxes impact
3. IT impact
4. Internal control impact
5. Key considerations for Ind AS conversion project
6. Key areas to be addressed during Ind AS conversion
7. Leveraging from the global experience
8. Ind AS conversion process

Direct tax impact

Ind AS are meant primarily to serve the needs of investors and therefore, are not suitable for the purposes of income tax computation. To address tax issues arising from Ind AS implementation, the Central Government (CG) had constituted a Committee in December 2010, to draft the Income Computation and Disclosure Standards (ICDS). Section 145 of the Indian Income tax Act bestows the power to the CG to notify ICDS to be followed by specified class of taxpayers or in respect of specified class of income.

Recently, the Government notified 10 ICDS effective from the current tax year itself (i.e., tax year 2015-16) for compliance by all taxpayers following mercantile system of accounting for the purposes of computation of income chargeable to income tax under the head “Profits and gains of business or profession” or “Income from other sources”. Though the ICDS are substantially aligned to the current Indian GAAP, there are few critical differences. Given below is an overview of key differences:

- ICDS I relating to accounting policies (corresponding to AS 1)
- ICDS I prohibits recognition of expected losses or mark-to-market losses unless permitted by any other ICDS.
- ICDS II relating to valuation of inventories (corresponding to AS 2)
Sale of standard cost method, as a technique for measurement of cost, is not permitted in ICDS II.

ICDS III relating to construction contracts (corresponding to AS 7)

During the early stages of a contract, where the outcome of the contract cannot be estimated reliably, contract revenue is recognized only to the extent of costs incurred. This requirement is contained both in AS 7 and ICDS III. However, unlike AS 7, ICDS III states that the early stage of a contract should not extend beyond 25% of the stage of completion.

AS 7 requires a provision to be made for the expected losses on onerous contract immediately on signing the contract. Under ICDS III, losses incurred on a contract will be allowed only in proportion to the stage of completion. Future or anticipated losses will not be allowed, unless such losses are actually incurred.

ICDS IV relating to revenue recognition (corresponding to AS 9)

Under AS 9 revenue from service transactions is recognized by following either the “percentage completion method” or the “completed contract method”. Under ICDS IV, only the percentage of completion method is permitted.

ICDS VI relating to the effects of changes in foreign exchange rates (corresponding to AS 11)

Under AS 11, all mark-to-market gains or losses on forward exchange or similar contracts entered into for trading or speculation contracts are recognized in P&L. In contrast, ICDS VI requires gains or losses to be recognized in the income computation only on settlement.

Under AS 11, exchange differences on a non-integral foreign operation are not recognized in the P&L, but accumulated in a foreign currency translation reserve. Such a foreign currency translation reserve is recycled to the P&L when the non-integral operation is disposed. Under ICDS VI, exchange differences on non-integral foreign operations will also be included in the computation of income.

ICDS VII relating to government grants (corresponding to AS 12)

Under AS 12, government grants in the nature of promoter’s contribution are equated to capital and hence are included in capital reserves in the balance sheet. Under ICDS VII, government grants should either be treated as revenue receipt or should be reduced from the cost of fixed assets based on the purpose for which such grant or subsidy is given.

Under AS 12, recognition of government grants should be postponed even beyond the actual date of receipt when it is probable that conditions attached to the grant may not be fulfilled and the grant may have to be refunded to the government. Under ICDS VII, recognition of Government grants cannot be postponed beyond the date of actual receipt.

ICDS VIII relating to securities (corresponding to AS 13)

Since ICDS deals with computation of income under Business or Other Sources heads, ICDS only deals with securities held as stock-in-trade.

Under both ICDS VIII and AS 13, securities should be valued at lower of cost or net realizable value (NRV). Under AS 13, current investments are carried in the financial statements at the lower of cost and fair value determined either on an individual investment basis or by category of investment. In contrast, ICDS requires that comparison of cost and NRV shall be done category-wise (and not for each individual security). Moreover, the categories specified in AS 13 and ICDS VIII are different.

Under ICDS VIII unlisted or thinly traded securities should be valued at cost.

Under ICDS VIII, cost which cannot be ascertained by specific identification should be determined on the basis of first-in- first-out (FIFO) method.

ICDS IX relating to borrowing costs (corresponding to AS 16)

Under AS 16 in the case of borrowings in foreign currency, borrowing costs include exchange differences to the extent they are treated as an adjustment to the interest cost. Under ICDS IX, borrowing cost will not include exchange differences arising from foreign currency borrowings.

AS 16 requires the fulfilment of the criterion “substantial period of time” for treating an asset as qualifying asset
for the purposes of capitalization of borrowing costs. ICDS retains substantial period condition (i.e. 12 months) only for qualifying assets in the nature of inventory but not for fixed assets and intangible assets. Therefore, ICDS requires capitalization of borrowing costs for tangible and intangible assets even when they are completed in a short period.

Under ICDS IX, capitalization of specific borrowing cost should commence from date of borrowing. Under AS 16, borrowing cost is capitalized from the date of borrowing provided the construction of the asset has started.

ICDS IX contains an allocation formula for capitalizing borrowing costs relating to general borrowings.

Unlike AS 16, income on temporary investments of borrowed funds cannot be reduced from borrowing costs eligible for capitalization in ICDS.

Unlike AS 16, requirement to suspend capitalization of borrowing costs during interruption of active construction of asset is removed in ICDS.

ICDS X relating to provisions, contingent liabilities and contingent assets (corresponding to AS 29)

Under ICDS X, a provision is recognized when it is “reasonably certain” that an outflow of economic resources will be required to settle an obligation. Under AS 29, the criterion is “probable”. In accounting literature, the term “reasonably certain” and “probable” generally indicate the same threshold levels.

Under ICDS X a contingent asset is recognized when the realization of related income is “reasonably certain”. Under AS 29 the criterion is “virtual certainty”.

It may be noted that ICDS are not tax neutral vis-à-vis the current Indian GAAP and tax practices currently followed and may give rise to litigation. For example, based on AS 7, the current practice is to recognize any expected loss on a construction contract as expense immediately. In contrast, ICDS will require expected losses to be provided for using the percentage of completion method.

ICDS I lays out the “accrual concept” as a fundamental accounting assumption. The prohibition on recognizing expected or mark-to-market losses appears to be inconsistent with the accrual concept. Though mark-to-market losses are not allowed to be recognized, there is no express prohibition on recognizing mark-to-market gains. The ICDS therefore, appear to be one sided, determined to maximize tax collection, rather than routed in sound accounting principles. Matters such as these are likely to create litigious situations.

The preamble of the ICDS states that where there is conflict between the provisions of the Income-tax Act, 1961 and ICDS, the provisions of the Income-tax Act will prevail. Consider that a company has claimed mark-to-market losses on derivatives as deductible expenditure under section 37(1) of the Income-tax Act. Can the company argue that this is a deductible expenditure under the Income-tax Act (though the matter may be sub judice) and hence should prevail over ICDS which prohibits mark-to-market losses to be considered as deductible expenditure?

Consider another example that a company receives government subsidy for non-depreciable asset. Hitherto, it was accepted that it is a capital receipt not falling within the definition of “income” and did not impact business income computation. Can the company argue that such receipt cannot be taxed in absence of amendment to definition of “income” and hence should prevail over ICDS which requires such receipt to be recognized as income over the period of meeting related obligations? These are untested areas, and could be litigated.

All ICDS (except ICDS VIII relating to Securities) contain transitional provisions. These transitional provisions are designed to avoid double jeopardy. For example, if foreseeable loss on a contract is already recognized on a contract at 31 March 2015, those losses will not be allowed as a deduction again on a go forward basis using the percentage of completion method. On the other hand, if only a portion of the loss was recognized, the remaining foreseeable loss can be recognized using the percentage of completion method. The detail
mechanism of how this will work is not clear from the ICDS. The transitional provisions are not always absolutely clear in all cases. In the case of non-integral foreign operations, e.g., non-integral foreign branches, ICDS requires recognition of gains and losses in the P&L (tax computation), rather than accumulating them in a foreign currency translation reserve. It is not absolutely clear from the transitional provision whether the opening accumulated foreign currency translation reserve, which could be a gain or loss, will be ignored or recognized in the first transition year 2015-16. Since the amounts involved will be huge, particularly for many banks, the interpretation of this transitional provision will have a huge impact for those who have not already considered the same in their tax computation in past years.

We understand that a CBDT committee is examining these issues. We recommend that companies must engage with these agencies to put their concerns in the forefront. It is imperative that companies identify and address these issues in a timely manner.

**MAT impact**

ICDS are meant for normal tax computation. Therefore, as things stand now, ICDS has no impact on minimum alternate tax (MAT) for corporate taxpayers, which will continue to be based on “book profit” determined under current AS or Ind AS, as the case may be.

The application of Ind AS will impact the calculation of book profits. Adopting Ind AS book profits as a starting point for computing MAT may have a significant impact on the MAT liability. In our view, a key issue is likely to arise regarding the payment of MAT on fair value gains recognized in the profit and loss account. In the absence of realized gains, paying taxes on such gains will strain companies’ cash flows. Moreover, issues will arise with regard to gains/losses adjusted to retained earnings in the opening Ind AS balance sheet in accordance with Ind AS 101. It is not clear whether these adjustments will be considered for MAT computation or they will permanently avoid MAT implications.

We believe that the regulators will need to consider the pros and cons of various approaches in deciding in final approach to be followed. The issue may become far more complicated if one were to consider that Ind AS is applicable on different dates based on the specified criteria’s, and for some entities, Ind AS does not apply. Overall, the Central Government through the Central Board of Direct Taxes (CBDT) will have to play a highly pro-active role to provide clarity and minimize the potential areas of litigation.

**Indirect taxes impact**

Currently, incidence of indirect tax and its computations is typically not based on treatment in the financial statements. However, in the past, tax authorities and courts have considered accounting treatment while deciding upon taxability. Therefore, the application of Ind AS may not have a direct implication on indirect tax computation; however, it may increase the possibility of litigation. This is because the application of Ind AS results in significantly different accounting in many cases. If the treatment as per Ind AS results in higher indirect tax payment, tax authorities may argue that the company should pay tax based on substance reflected in the financial statements. The following are a few examples in this regard:

1. **Under Ind AS**, a BOT operator recognizes a financial asset or intangible asset, as the case may be, in lieu of its investment in developing the infrastructure. This is accounted for as though the operator provides construction services to the grantor and, in exchange, receives a financial asset or an intangible asset at fair value, i.e., cost plus margin. Under indirect tax laws, there have been recent judicial pronouncements contending that the operator in a BOT contract can be construed as a “dealer” for the purpose of assessment of VAT/works contract tax. The application of Ind AS accounting may further strengthen the argument of indirect tax authorities that the operator needs to pay works contract tax on such construction revenue.

2. Application of Ind AS may require companies to identify and account for separately leases embedded in transactions structured as sale or purchase or service. For example, a manufacturing company will need to analyze its exclusive sale/purchase agreement for embedded leases. Under Indian GAAP, such arrangement is typically accounted for as sale/purchase of goods and sales tax/VAT is payable on the sale. However, if the company determines that the agreement contains a lease, it may raise an issue on whether it needs to pay service tax on lease rent? If yes, what will be the position on sales tax/VAT?

3. **Under Ind AS**, companies may need to split composite contracts into various elements and allocate proportionate value toward items such as service element and other free items. Will tax authorities consider such split for calculation of sales tax and service tax liabilities? What will happen if such split results into recognition of revenue at an earlier stage than when the bill is actually raised? Will tax liability be also correspondingly advanced?
4. In case of sale on deferred payment terms, a company will recognize sale at fair value of consideration receivable. If Ind AS financial statements are used for tax purposes, will the tax authorities accept fair value consideration for computation of excise duty/sales-tax liability or these liabilities will continue to be determined based on invoice amount? Will deduction of tax at source (TDS) requirement apply on finance cost/finance income in recognized in this manner?

Further, there are certain BOT operators who have entered into revenue-sharing arrangement with the government. In the intangible asset model, a BOT operator recognizes revenue twice: once construction revenue on construction of the infrastructure and later, toll revenues. In such cases, there can be an issue on whether they are required to share revenue twice with the government?

It is recommended that the government clarifies that it will maintain a tax neutral position with respect to indirect taxes and other levies.

**IT impact**

Information technology (IT) is likely to play a substantial role in the process of converting to Ind AS. It is advisable not to underestimate the time and effort the conversion process will require, or the inherent potential risks. A well-planned process is critical for converting successfully while controlling costs, maintaining reporting integrity, and avoiding potential financial restatements or other surprises.

The adoption of Ind AS requires changes in the recognition, measurement and disclosure of many items in the financial statements. Both financial and business systems need to deliver the information required for compliance with Ind AS. Accordingly, IT systems will need to be modified so that the financial data produced conform to Ind AS. It is important to note that such changes are not restricted to IT modules relating to general ledger entries or sub-ledger entries, but also affect applications such as asset management systems, financial instruments and payroll systems. Our experience with global IFRS conversions has shown there are four main drivers that determine the scale of an IT project.

The main driver for system- and IT-related changes is how the new accounting standards are to be applied. The impact will be influenced by the existing financial reporting processes and the industry in which an entity operates. For example, the new reporting requirements regarding property, plant and equipment will likely be far more difficult to implement if an entity operates in a capital-intensive industry. Similarly, an entity with significant assets/liabilities, requiring the use of fair values, would need to specifically focus on the computation of fair values. When an active market does not exist for the measurement of fair value, the entity will have to use other more complex valuation techniques. In such an event, IT systems need to be able to capture the data required for such valuations.

An entity’s finance team needs to work closely with its IT team to understand the system-related impact of Ind AS requirements. Conducting a diagnostic impact assessment at the beginning of a project will help to identify the differences between existing accounting policies and practices and those required under Ind AS. We recommend that the IT department takes part in this assessment to identify affected systems and required modifications early in the process. This will also help organizations to effectively implement changes to best suit their infrastructure and systems.

System changes from Ind AS are generally classified into three main types:

- **Data changes**: Ind AS can create additional data requirements. For example, fixed assets must be broken down by significant components to apply component accounting more comprehensively under Ind AS. This may require the creation of new asset types and definitions of the useful life of each asset. Separate master data can be maintained to track useful lives, depreciation rates and amounts, which requires extensive data conversion and mapping of historical data.

- **System configuration/parameter changes**: Ind AS may change existing system configurations and routines, e.g., identification of multiple element contracts.

- **Reporting changes**: Ind AS differences will have an impact on reporting tools and reports. For example, the manner in which revenue is determined under Ind AS for contracts involving deferred payments may be substantially different from the existing practice in India. This difference will have a substantial impact on reports relating to revenue.

Though Ind AS is applicable from 1 April 2016 for companies covered under the mandatory phase 1, comparable data will be required for the financial year 2015-16. In other words, for the period 2015-16, the system will have to support dual reporting, i.e., Indian GAAP for statutory reporting and Ind AS for keeping comparable data ready. Perhaps the most significant impact may be determining how the systems will support the dual-reporting requirement for the period 2015-16. This may require an entity to maintain two parallel charts of accounts. We believe that some systems, such as new releases of enterprise...
resource planning (ERP) packages, may provide dual-reporting functionality. In other cases, the entities may undertake the application upgrades or the implementation of new applications or modules to handle dual reporting through their IT systems. Alternatively, the information may need to be handled outside the IT systems. This can be done manually or by using short-term solutions in the initial period. What approach is best would be determined by the scale of changes required by Ind AS and the extent of IT automation, resource and cost considerations.

**IT organization structure**

Our experience with IFRS conversion shows us that the structure of an IT function may have a significant impact on the resources required to implement Ind AS. For example, if an entity has a centralized IT function, a focused IT Ind AS project team can probably make the required system or IT process changes from a single location. However, if the IT function is decentralized across multiple locations and business units, the number of affected people, systems, business units and processes could be significant. IT personnel would also need some training to understand Ind AS requirements and their impact on IT systems.

**Existing IT system plans**

Ind AS can have a direct impact on an entity's system plans, particularly on financial system implementations or upgrades. If an entity has other large system projects on the horizon, it would be better to identify interdependencies within the Ind AS project and manage resources appropriately.

If an entity is implementing or upgrading financial systems in parallel with the Ind AS project, the finance team may have to make assumptions regarding functional system requirements during the design phase of the upgrade or implementation. Close co-ordination between the finance, IT and the systems implementation teams is critical. We recommend that the Ind AS project team has a representative from the systems implementation team.

**Application architecture**

The general rule of thumb is “simpler the application architecture, easier would be the implementation”. Typically, conversion in a single-ERP environment is relatively straightforward. Our experience shows that the complexity and effort increase greatly if an entity has multiple ERPs or customized applications supporting the financial processes.

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**Internal control impact**

The requirement to maintain effective internal control throughout the conversion process cannot be over-emphasized. The Companies Act 2013, as well as the listing agreement, require a company to ensure existence as well as operating effectiveness of internal financial control:

- Clause 49 of the Listing Agreement, among other matters, requires that CEO/CFO will certify to the board that they accept responsibility for establishing and maintaining internal controls for financial reporting and that they have evaluated the effectiveness of internal control systems of the company pertaining to financial reporting.
- The Companies Act 2013 requires the board to state that directors have laid down internal financial controls, such controls are adequate and were operating effectively.
- Under the Companies Act 2013, the auditor’s report, among other matters, should state “whether the company has adequate internal financial controls system in place and the operating effectiveness of such controls.”

In most cases, transition to Ind AS will require significant changes in an entity's financial reporting framework. This may cause significant changes in underlying processes and controls and thereby increase the risk of error or fraud. Companies will need to consider whether adequate controls are in place to address Ind AS conversion challenges. They may also need to modify its control strategy to reflect changed risk assessments. Given below are few example of impact on control consideration arising from Ind AS application:

- Under Ind AS, separate accounting for components of PPE is more rigorously and more broadly applied. To ensure the same, controls over the componentization of assets may be required. Controls with respect to reviewing judgments over both the identification of significant components and the assignment of costs to components, including borrowing costs, will be required. Additional amortization categories may affect configuration of the fixed asset sub-ledger. Controls over system changes may need to be considered prior to any significant changes.
Ind AS 101 allows entities to elect to measure individual items of PPE, including leased assets under a finance lease, at fair value at the date of transition to Ind AS. The fair value becomes the deemed cost at that date, with the corresponding adjustment being booked to retained earnings in the opening Ind AS balance sheet. Where appraisals will be conducted, controls need to ensure that an appropriately qualified individual conducts any appraisal. Controls are also needed over the inputs and outputs provided to the appraiser and the review of the work, including assumptions, of the appraiser.

Ind AS 37 requires that all provisions be discounted where the effect of time value is material. It also requires re-measurement of provisions at the end of each reporting period for changes in the discount rate. Appropriate change management controls are required for the appropriate selection of a discount rate each period. Controls are also required over the revaluation of obligation each period.

We may emphasize that these considerations are illustrative only and specific control impacts will depend on the facts and circumstances of each entity. In deciding control impacts, the entity should also address the following key aspects:

- Some entities engage external advisers or their auditors to assist management in Ind AS conversion. In these cases, controls should be implemented over the proper exchange of information with the advisers. Also, the senior management should appropriately review the assumptions and recommendations of the adviser. Appropriate senior members of management must oversee the consultation process and conduct a judicious review of the final recommendations before making accounting policy decisions for the entity.

- Accounting policy and elective exemption decisions should be approved by management on a timely basis. The entity’s audit committee should be involved in the process well ahead of the transition date and before the entity begins to apply the new policies.

In accordance with Ind AS 101, the first Ind AS financial statements should include comparative reconciliations between Ind AS and the previous GAAP. Controls should be in place over both the creation of the opening balance sheet and the reconciliation process. We believe that the reconciliations are most transparent and informative when done on a line-by-line basis. The nature of the controls over the reconciliation process will depend on the number of reconciling adjustments expected and how an entity chooses to track its accounting records concurrently under Ind AS and the previous GAAP.

If possible, the entities should conduct control testing earlier than the due date. This approach may contribute to both efficiency and effectiveness by reducing resource constraints at the time of transition, allowing for early detection and remediation of control failure issues. This will also facilitate interviews of individuals involved in the conversion process while the details are still fresh.
Key considerations for Ind AS conversion project

The conversion to Ind AS presents potential opportunities that companies may want to further examine and explore. Many companies operate on a global scale and have competitors that are not based out of India. Being able to provide financial reports to investors and other interested parties based on the same/similar accounting standards used by those peers may increase the company’s comparability with its peers.

Once the conversion commences, companies may want to understand the financial reporting decisions being made by their peers and other companies around exemptions/relaxations given on first-time adoption. This will require converting companies to share their thoughts and perspectives on potential policies with each other. Notably, companies that have already adopted IFRS in Europe, Australia or elsewhere can provide useful information. Further, investors and market analysts will also want to be aware of the choices that the company is making and how these choices compare against the ones made by the company's peers.

Some companies will realize that there is a significant underlying opportunity in using the conversion project as a means to drive other areas of change. For example, companies may consider the conversion to Ind AS as an opportunity to streamline accounting and reporting processes or to accelerate the financial statement close process.

Along with opportunities, there are many potential risks also attached with Ind AS conversion process. Conversion to Ind AS will be one of the most fundamental changes in financial reporting in the Indian history. The potentially pervasive nature of the changes at the accounting, functional, transactional and internal control levels also increases the risk of misstatement. Further, the current financial reporting environment has little tolerance for mistakes, and it will be important for all companies to get the conversion right in the first time. Misstatements, as well as missed reporting deadlines, present a significant risk to companies that are converting.

There are various risks associated with the conversion to Ind AS that will have to be addressed by the management. The examples of potentially significant risk areas include:

- Failure to communicate the effects and results to stakeholders, including boards, audit committees, investors and analysts
- Accounting and reporting under multiple accounting frameworks during the transition period
- Maintaining consistency in the manner in which the various Ind AS principles are applied throughout the organization, including the potential to have to rethink accounting policy decisions made by subsidiaries who have already adopted Ind AS or their equivalents
- Retention of key employees
- Excessive costs brought on by ineffective planning, project management and/or rework
- Unreasonable or excessive work levels, brought on by inappropriate planning or unreasonable expectations
- Missed deadlines in the conversion timetable
- Inability of the CEO/CFO/Board/auditor to conclude and certify on the effectiveness of the company’s internal controls over financial reporting as required under the Listing Agreement/Companies Act 2013

To mitigate these risks, the boards should pay close attention to the details of the management’s approach for Ind AS conversion and satisfy themselves that it covers all appropriate areas, and is based on sound project management principles. While the management will be responsible for the conversion execution, boards need to be confident in the management’s plan, thoroughness and diligence. Management should inform the board and the audit committee on a regular basis as to its plan and progress. As such, audit committees should typically include a standing Ind-AS agenda update item at their periodic meetings.
Key areas to be addressed during Ind AS conversion

No two Ind AS conversion projects will ever be the same. However, while the specific issues that the companies will face during their conversion will vary widely because of all the variables at play, the key areas that the management and boards will need to address during the conversion should be broadly similar.

1. **Project launch and planning activities:** The initial decisions made during the project set-up phase tend to be crucial for eventual project success. These decisions include:
   a) Creating a project management function to coordinate project activity and monitor/report progress
   b) Structuring the project team based on the results of the impact assessment phase
   c) Assigning sufficient resources to the project and determining that the team comprises individuals with appropriate skills to fulfil their responsibilities

2. **Revision of accounting policies:** Reassessing accounting policies under Ind AS will be one of the most important elements of the project because decisions made in this area will drive many of the changes required throughout the business and will have direct implications for the future business results. For instance, accounting policy decisions will affect data collection requirements, which, in turn, will affect IT system requirements, business processes to collect and record the data, internal control systems covering data validity and functional resourcing requirements. The tax-related effects of revisions of accounting policies will also need to be addressed in the conversion process. Audit committees and boards will need to review and be comfortable with the policies selected by management.

3. **Application of Ind AS 101:** Another key area that the management will need to address with respect to accounting policies is how it will apply Ind AS 101. Ind AS 101 provides guidance for businesses on how to adopt Ind AS for the first time and provides companies with a number of voluntary exemptions and mandatory exceptions from the requirements of other standards. The decisions made in applying Ind AS 101 will often have a significant effect on the financial statements for many years to come.

4. **Development of skeleton financial statements compliant with Ind AS:** Companies will have to redraft the sections of their financial statements to meet Ind AS disclosure requirements. There are multiple benefits in preparing a skeleton set of financial statements during the preliminary phases of the project as it focuses attention on the actual disclosure requirements of the business, and therefore, is crucial in the process of identifying “data gaps” that need to be plugged. It is also useful to put the overall change management challenge in perspective and give project teams a concrete goal.

5. **Preparation/restatement of financial information from Indian GAAP to Ind AS for comparative accounting periods:** The compilation of comparative financial information for inclusion in the first set of Ind AS financial statements may prove to be one of the most challenging areas of the project. The board, through its audit committee, needs to be satisfied as to whether careful consideration has been given to the approach adopted by the management to compile this information.

6. **Transition approach:** While some companies outside the India converted “top-side” only at a consolidated level, this spreadsheet approach is not ideal. Accounting treatments and controls should be pushed down to the subsidiary and transaction level. This will be very useful in compiling relatively more accurate data and maintaining effective control. Further, the spreadsheet approach may not work in long term. The audit committee will need to carefully consider and opt for the transition approach that is more appropriate and better suited to its business.

7. **Identifying and resolving data capture issues:** The increased level and complexity of certain financial disclosures expected under Ind AS may require significant project resources to identify and set up processes to collate this data. Some of the data underlying the new disclosures may be time consuming to extract or may need significant analysis before it is ready for disclosure purposes. Boards need to be satisfied that the management’s plans include adequate mechanisms to identify and resolve data gaps.
8. **Retraining of personnel:** Boards need to be satisfied in terms of adequate investment being made in retraining employees throughout the organization in order to meet their changed technical knowledge needs, as well as be equipped to facilitate the roll out of accounting policy changes and the associated revised business processes and procedures.

9. **Communication with stakeholders:** Managing investors’ and other stakeholders’ expectations with respect to the impact of Ind AS and the company’s progress toward conversion will be an important area for boards to monitor. Clear, continuous and consistent communication with stakeholders will reduce the risk of misunderstandings and aid a smooth transition.

10. **Audit committee financial literacy and retraining:** The training requirements will also apply to members of the audit committee. Whether trained through management briefings or by outside parties, audit committee members should have sufficient knowledge about Ind AS to be able to evaluate management’s assessments and selection of accounting policies.
## Leveraging from the global experience

Indian businesses have the benefit of the experience of countries that have already converted to IFRS. We have detailed some of the issues encountered and the key lessons one can learn from their experiences in the following table:

<table>
<thead>
<tr>
<th>Issues identified</th>
<th>Key lessons learnt</th>
</tr>
</thead>
<tbody>
<tr>
<td>The scale and complexity of the project and the time frame needed were underestimated.</td>
<td>Conducting a thorough impact assessment, followed by a detailed planning exercise up front, is crucial for a successful transition. Conversions could entail functional changes as well as technical accounting changes.</td>
</tr>
<tr>
<td>The project lacked adequate buy-in from the company’s senior management early on in the project.</td>
<td>The “tone from the top” is an important driver of change. The board sponsorship of the project is crucial.</td>
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<tr>
<td>The projects suffered from poor project management.</td>
<td>The importance of having a proper project management office function capable of coordinating project activities and a well-structured conversion methodology cannot be overemphasized.</td>
</tr>
<tr>
<td>Slight accounting differences can have a significant effect on financial results.</td>
<td>A methodical approach to review accounting differences is essential to assess the overall financial impact.</td>
</tr>
<tr>
<td>Unfamiliarity of “numbers” and principles arising from changes.</td>
<td>Technical training will be a critical component of the conversion, especially for business unit heads, who may not be familiar with the implications of the changes that new standards will bring. Investor relations will also need a strong educational grounding to communicate the impact to investors.</td>
</tr>
<tr>
<td>Poor communication existed between project team and business units regarding effects of changes.</td>
<td>Invest the time necessary to roll out business process changes such as accounting practices, updated control mechanisms and changes in reporting requirements to the wider organization.</td>
</tr>
<tr>
<td>Changes were often not fully embedded in back offices and general ledger systems.</td>
<td>EU companies that used manual workarounds to meet short deadlines have to subsequently redesign processes and augment their systems to eliminate the inefficiencies these workarounds created. Indian companies should use the time available to proactively address these changes.</td>
</tr>
<tr>
<td>The top-side solutions did not work.</td>
<td>The top-side solutions do not cause the organization to adjust, and the finance group feels “all the pain.” It is important to “push down” the conversion to the transaction level throughout the organization as early as possible.</td>
</tr>
<tr>
<td>Tax personnel were frequently underrepresented in the conversion process.</td>
<td>The tax implications of the conversion process may extend beyond accounting effects. The early involvement of tax personnel in the process may mitigate potential for unexpected results. Companies will benefit from sufficient resources and adequate lead time to address tax issues and to make necessary changes to tax processes and technology.</td>
</tr>
</tbody>
</table>
Ind AS conversion process

In an Ind AS conversion, an entity undertakes to change its financial reporting from its current GAAP (Indian GAAP for most Indian companies) to Ind AS. Obviously, differences between the Indian GAAP treatment and Ind AS would be one of the key inputs to the conversion process in case of Indian companies. These differences may vary significantly from one company to another depending on the industry and the current accounting policies chosen under Indian GAAP. However, the magnitude of an Ind AS conversion project will not depend solely on the magnitude of the GAAP differences, but will be influenced by other factors such as:

- The quality and flexibility of the existing financial reporting infrastructure,
- The size and complexity of the organization, and
- The effect of GAAP changes on the business.

Ultimately, the purpose of an Ind AS conversion is to put companies in a position where they are able to report, unaided and reliably, under Ind AS and are able to recognize the Ind AS dimension of their actions. However, before the actual start of the conversion project, an initial diagnostic phase should put companies in a position where they are aware of:

- The differences between Ind AS and the company’s current accounting policies,
- The impact of the change to Ind AS on the financial statements,
- The impact of the change to Ind AS on tax, business IT and process,
- The impact of Ind AS on future business decisions, and
- An understanding of the approach underlying the formulation of Ind AS.

Need for conversion methodology

Many companies perceive conversion projects purely as a technical accounting exercise. With a major underlying difference of principle — as embodied in Ind AS— this is a grave mistake. Ind AS conversions, if not properly planned, are likely to lead to a number of unfortunate results. Common among these are:

- Failure to involve all people with the required knowledge, business decisions taken in ignorance of the financial reporting consequences, unreliability and slowness in producing Ind AS financial statements, and
- Gross underestimation of the time required to convert.

Conversion to Ind AS will be an exercise in change management. Adopting Ind AS may affect many facets of an organization beyond its financial reporting. Every aspect of a company affected by financial information has the potential for change (for example, key performance indicators, employee and executive compensation plans, management’s internal reporting, investor relations and analyst information). Both the process and the implications of the conversion can vary widely among companies based on a number of variables, such as levels of expertise, degree of centralization of accounting processes and data collection, and the number of existing accounting methods currently being used. Often, information and data not currently collected and/or warehoused may be needed to produce the required Ind AS information.

The conversion to Ind AS will entail a business wide change management exercise and should be approached using a structured methodology encompassing the best practices of project management. Such methodology ensures conversion assignments are properly planned and executed. The methodology also ensures that the typical pitfalls for the inexperienced conversion team are avoided by:

- Promoting the re-use of knowledge,
- Avoiding costly dead-ends resulting from poor planning and co-ordination,
- Ensuring efficient use of staff time,
- Allowing a mix of experienced and less experienced staff, thereby, facilitating knowledge transfer, and
- Improving the quality of the work.
To take full advantage of the opportunities arising as a result of conversion to Ind AS, the conversion methodology needs to be flexible and customized to the needs of a company. As with any major finance transformation project, the full support of the board and senior management will be critical to the success of the conversion effort. Boards should pay close attention to the details of management’s proposed approach to the Ind AS conversion to satisfy themselves that it covers all appropriate areas and is based on sound project management principles. While management will be responsible for the conversion execution, boards need to be confident in management’s plan, thoroughness and diligence. Management should inform the board and the audit committee on a regular basis as to its plan and progress. As such, audit committees should generally include a standing Ind AS agenda update item at their periodic meetings.

The process

A sample methodology for conversion is shown above, which management may consider for Ind AS conversion.

The methodology takes, as a starting point, the fact that an Ind AS conversion project needs to address more than just accounting issues and that a conversion project is sufficiently complicated to warrant professional project management. It is for these reasons that the methodology comprises five phases, each of which deals with a specific part of the conversion, and that throughout the project it recognizes five different workstreams, each dealing with a specific aspect of the conversion process. This is to facilitate involvement of specialists on need basis. It is, however, important to recognize that the phases can overlap one another and entities need not wait for completion of one phase to end before beginning another. Also, a clear breakdown of all the activities by workstream is not always possible as a mandatory allocation of activities by phase. Thus, this methodology should be tailored according to project specificities, starting point and in place project structure, etc.
Key goals and outputs of each phase

**Diagnostic**

This phase involves high level identification of accounting and reporting differences and the consequences to the business, IT, processes and tax. The major outcome management should expect from this phase includes an impact assessment report, which provides implications on above areas. It also entails determining a high-level roadmap for future phases of the conversion. This phase will also help management to identify potential interdependence between the Ind AS conversion project and current or planned organization-wide initiatives (for example, new accounting system implementations such as ERP and finance transformations) and an assessment of, whether the company has adequate resources to complete a conversion.

**Design and planning**

This phase involves setting up the project infrastructure, the project management function, including conversion roadmap and change management strategy. The aim of this phase is to set-up a core Ind AS team, framing conversion time-tables and deciding on detailed way-forward. Formation of the project structure, project charter, communication plan, training plan and expanded conversion roadmap are typical outputs from this phase.

**Solution development**

The objective of this phase is to identify solutions to various issues identified in relation to accounting and reporting, tax, business process and system changes. Typical outputs from this phase comprise of Ind AS accounting manuals, group reporting packages, Ind AS skeleton financial statements, group accounting policies, technical papers on Ind AS accounting issues, crystallizing the impact on current and deferred tax, developing solutions for tax functions and identifying processes which need to be re-designed, modified or developed.

**Implementation**

This phase involves roll out of solutions developed in the previous phase. In this phase the company will conduct a process of dry-run of financial statements to ensure that before the reporting deadline, company is geared up to prepare Ind AS financial statements. Post dry-run financial statements, the company will roll-out final deliverables, i.e., the opening Ind AS balance sheet and the first Ind AS financial statements. All business and process solutions developed will also be implemented to facilitate the company transition to the new reporting framework.

**Post-implementation**

This phase involves an assessment of how various solutions developed work in the implementation phase and the identification of any issues in the operational model. These issues are tackled in this phase to ensure successful on-going functioning of systems and processes in Ind AS reporting regime. On-going update training is also provided, to ensure that company’s personnel are updated with latest Ind AS developments, and also changes are made in systems and processes. Ind AS manuals will also need to be regularly updated for changes in Ind AS.
Appendix: Sample Ind AS reconciliation note for first Ind AS financial statements

This Appendix presents an illustrative example of the reconciliation disclosures required by Ind AS 101 using a fictional company, FTA Limited (“FTA” or “the company”). The example assumes that FTA Group’s first Ind AS financial statements are for the year ended on 31 March 2017, with a transition date of 1 April 2015. FTA prepared Indian GAAP annual financial statements for the year ended 31 March 2016.

The intent of the example is to illustrate the periods to be reconciled and the type of disclosures required to explain the related adjustments. The example is not comprehensive and is not intended to reflect all possible accounting entries that would be necessary for a first-time adopter.

First-time adoption of Ind AS

FTA Group’s consolidated financial statements (CFS) for the year ended 31 March 2017 are the first annual financial statements which the Group has prepared in accordance with Ind AS. For periods up to and including the year ended 31 March 2016, the Group prepared its CFS in accordance with Indian GAAP, including accounting standards notified under section 133 of the Companies Act 2013 read together with paragraph 7 of the Companies (Accounts) Rules, 2014.

Accordingly, the Group has prepared CFS, which comply with Ind AS applicable for periods ending on or after 31 March 2017, together with the comparative period data as at and for the year ended 31 March 2016, as described in the summary of significant accounting policies. In preparing the CFS, the Group’s opening balance sheet was prepared as at 1 April 2015, the Group’s date of transition to Ind AS. This note explains the principal adjustments made by the Group in restating its Indian GAAP CFS, including the balance sheet as at 1 April 2015 and the CFS as at and for the year ended 31 March 2016.
Exemptions applied

Ind AS 101 allows first-time adopters certain exemptions from the retrospective application of certain requirements under Ind AS. The Group has applied the following exemptions:

- The Group has elected that it will not apply Ind AS 103 Business Combinations retrospectively to business combination (including acquisitions of subsidiaries that are considered businesses for Ind AS, or of interests in associates and joint ventures) occurring before 1 April 2014. Use of this exemption implies that Indian GAAP carrying amounts of assets and liabilities, which are required to be recognized under Ind AS, is their deemed cost at the date of the acquisition. After the date of the acquisition, measurement is in accordance with Ind AS. Assets and liabilities that do not qualify for recognition under Ind AS are excluded from the opening Ind AS balance sheet. The Group did not recognize or exclude any previously recognized amounts as a result of Ind AS recognition requirements.

- Ind AS 101 also requires that Indian GAAP carrying amount of goodwill must be used in the opening Ind AS balance sheet (apart from adjustments for goodwill impairment and recognition or derecognition of intangible assets). In accordance with Ind AS 101, the Group has tested goodwill for impairment at the date of transition to Ind AS. No goodwill impairment was deemed necessary at 1 April 2015. The group has used same exemptions for acquisition of interests in associates and joint ventures

- However, the Group has applied Ind AS 103 to business combinations occurring on or after 1 April 2014. The Group has acquired only one business on slump sale basis during the period beginning 1 April 2014 and ending before the transition date.

- As part of the business combination exemption, the group has also used Ind AS 101 exemption regarding previously unconsolidated subsidiaries. The use of this exemption requires the group to adjust the carrying amounts of the previously unconsolidated subsidiary’s assets and liabilities to the amounts that Ind AS would require in the subsidiary’s balance sheet. The deemed cost of goodwill equals the difference at the date of transition to Ind AS between (i) the parent’s interest in those adjusted carrying amounts, and (ii) the cost in the parent’s separate financial statements of its investment in the subsidiary. The cost of a subsidiary in the parent’s separate financial statements is the Indian GAAP carrying amount at the transition date.

- The Group has not applied Ind AS 21 retrospectively to fair value adjustments and goodwill from business combinations that occurred before 1 April 2014, which is also the cut-off date for the use of business combination exemption. Such fair value adjustments and goodwill are treated as assets and liabilities of the parent rather than as assets and liabilities of the acquiree. Therefore, those assets and liabilities are already expressed in the functional currency of the parent or are non-monetary foreign currency items and no further translation differences occur.

- Freehold land and buildings, other than investment property, were carried in the balance sheet prepared in accordance with Indian GAAP on the basis of valuations performed on 31 March 2014. The Group has elected to regard those values as deemed cost at the date of the revaluation since they were broadly comparable to fair value.

- Certain items of property, plant and equipment have been measured at fair value at the date of transition to Ind AS. The fair value so determined is deemed cost for these items of property, plant and equipment.

- Since there is no change in the functional currency, the group has elected to continue with the carrying value for all of its investment property as recognized in its Indian GAAP financial as deemed cost at the transition date.

- Cumulative currency translation differences for all foreign operations are deemed to be zero as at 1 April 2015, i.e., date of transition to Ind AS.

- Ind AS 102 Share-based Payment has not been applied to equity instruments in share-based payment transactions that vested before the date of transition to Ind AS. For cash-settled share-based payment transactions, the Group has not applied Ind AS 102 to liabilities that were settled before the date of transition to Ind AS.

- Appendix C to Ind AS 17 requires an entity to assess whether a contract or arrangement contains a lease. In accordance with Ind AS 17, this assessment should be carried out at the inception of the contract or arrangement. However, the Group has used Ind AS 101 exemption and assessed all arrangements for embedded leases based on conditions in place as at the date of transition.

- The Group has designated equity instruments held for purposes other than trading as at fair value through OCI investments. This designation is made on the basis of facts and circumstances existing at the date of transition to Ind AS.
The group has applied Ind AS 115 retrospectively. In applying Ind AS 115 retrospectively, it has used the following practical expedients:

- For completed contracts, the group has not restated contracts that begin and end within the same annual reporting period;
- For completed contracts that have variable consideration, the group has used the transaction price at the date when the contract was completed rather than estimating variable consideration amounts in the comparative reporting periods; and
- For all reporting periods presented before the beginning of the first Ind AS reporting period, the group has not disclosed the amount of the transaction price allocated to the remaining performance obligations and an explanation of when the group expects to recognize that amount as revenue.

The key impact of retrospective application of Ind AS 115 relates to accounting for customer loyalty program.

**Estimates**

The estimates at 1 April 2015 and at 31 March 2016 are consistent with those made for the same dates in accordance with Indian GAAP (after adjustments to reflect any differences in accounting policies) except for the items where application of Indian GAAP did not require similar estimation. The estimates used by the Group to present these amounts in accordance with Ind AS reflect conditions at 1 April 2015 the date of transition to Ind AS and as of 31 March 2016.

**Hedge accounting**

The Group uses derivative financial instruments, such as forward currency contracts, interest rate swaps and forward commodity contracts, to hedge its foreign currency risks, interest rate risks and commodity price risks, respectively. Under Indian GAAP, there is no mandatory standard that deals comprehensively with hedge accounting. The group has designated various economic hedges and applied economic hedge accounting principles to avoid profit or loss mismatch. All the hedges designated under Indian GAAP are of types which qualify for hedge accounting in accordance with Ind AS 109 also. Moreover, the group, before the date of transition to Ind AS, has designated a transaction as hedge and also meets all the conditions for hedge accounting in Ind AS 109. Consequently, the group continues to apply hedge accounting after the date of transition to Ind AS.

**Government loans**

The Group has classified government loan received as a financial liability in accordance with the principles of Ind AS 32. The Group has applied the requirements in Ind AS 109 prospectively to government loans existing at the date of transition to Ind AS. Hence, the Group has not recognized the corresponding benefit of the government loan at a below-market rate of interest as a government grant.
Group Reconciliation of equity as at 1 April 2015 (date of transition to Ind AS)

<table>
<thead>
<tr>
<th>Footnotes</th>
<th>Indian GAAP</th>
<th>Adjustments</th>
<th>Ind AS</th>
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</thead>
<tbody>
<tr>
<td><strong>Equity and liabilities</strong></td>
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<tr>
<td><strong>Equity</strong></td>
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<td>Equity share capital</td>
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<tr>
<td>Other equity</td>
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<tr>
<td>Equity component of convertible preference shares</td>
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<tr>
<td>Securities premium</td>
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<td>Reserve representing unrealised gains/losses</td>
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<td>Other reserve</td>
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<td>Equity attributable to equity holders of the parent</td>
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<td>Non-controlling interests</td>
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<td>Financial Liabilities</td>
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<td>Interest-bearing loans and borrowings</td>
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<tr>
<td>Other non-current financial liabilities</td>
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<td>Long term provisions</td>
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<td>Deferred tax liabilities</td>
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<td><strong>Financial Liabilities</strong></td>
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<td>Trade and other payables</td>
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<td>e</td>
<td>XXX</td>
<td>XXX</td>
</tr>
<tr>
<td>Government grants</td>
<td></td>
<td>XXX</td>
<td></td>
</tr>
<tr>
<td>Deferred revenue/ Contract liability</td>
<td>p</td>
<td>XXX</td>
<td></td>
</tr>
<tr>
<td>Income tax payable</td>
<td></td>
<td>XXX</td>
<td></td>
</tr>
<tr>
<td>Provision</td>
<td>o</td>
<td>XXX</td>
<td></td>
</tr>
<tr>
<td>Liabilities directly associated with the assets classified as held for distribution</td>
<td></td>
<td>XXX</td>
<td>XXX</td>
</tr>
<tr>
<td><strong>Total liabilities</strong></td>
<td></td>
<td>XXX</td>
<td>XXX</td>
</tr>
<tr>
<td><strong>Total equity and liabilities</strong></td>
<td></td>
<td>XXX</td>
<td>XXX</td>
</tr>
<tr>
<td><strong>Assets</strong></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td><strong>Non-current assets</strong></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Property, plant and equipment</td>
<td>c, d, i, m</td>
<td>XXX</td>
<td></td>
</tr>
<tr>
<td>Investment properties</td>
<td></td>
<td>XXX</td>
<td></td>
</tr>
<tr>
<td>Intangible assets</td>
<td></td>
<td>XXX</td>
<td></td>
</tr>
<tr>
<td>Investment in an associate/ joint venture</td>
<td>c, d</td>
<td>XXX</td>
<td></td>
</tr>
<tr>
<td>Other non-current financial assets</td>
<td>s</td>
<td>XXX</td>
<td></td>
</tr>
<tr>
<td>Deferred tax assets</td>
<td></td>
<td>XXX</td>
<td></td>
</tr>
<tr>
<td><strong>Current assets</strong></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Inventories</td>
<td>c</td>
<td>XXX</td>
<td></td>
</tr>
<tr>
<td>Financial assets</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Trade and other receivables</td>
<td>f</td>
<td>XXX</td>
<td></td>
</tr>
<tr>
<td>Other current financial assets</td>
<td>g</td>
<td>XXX</td>
<td></td>
</tr>
<tr>
<td>Cash and short-term deposits</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Prepayments</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Assets classified as held for distribution</td>
<td></td>
<td>XXX</td>
<td></td>
</tr>
<tr>
<td><strong>Total assets</strong></td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>
## Group reconciliation of equity as at 31 March 2016

<table>
<thead>
<tr>
<th></th>
<th>Footnotes</th>
<th>Indian GAAP</th>
<th>Adjustments</th>
<th>Ind AS</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Equity and liabilities</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td><strong>Equity</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Equity share capital</td>
<td></td>
<td>XXX</td>
<td>XXX</td>
<td>XXX</td>
</tr>
<tr>
<td>Other equity</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Equity component of convertible preference shares</td>
<td>q</td>
<td>XXX</td>
<td>XXX</td>
<td>XXX</td>
</tr>
<tr>
<td>Treasury shares</td>
<td></td>
<td>XXX</td>
<td>XXX</td>
<td>XXX</td>
</tr>
<tr>
<td>Retained earnings</td>
<td>a, b, q i, q</td>
<td>XXX</td>
<td>XXX</td>
<td>XXX</td>
</tr>
<tr>
<td>Reserve representing unrealised gain/losses</td>
<td>i, k</td>
<td>XXX</td>
<td>XXX</td>
<td>XXX</td>
</tr>
<tr>
<td>Other Reserve</td>
<td>i, q, k</td>
<td>XXX</td>
<td>XXX</td>
<td>XXX</td>
</tr>
<tr>
<td><strong>Equity attributable to equity holders of the parent</strong></td>
<td>XXX</td>
<td>XXX</td>
<td>XXX</td>
<td></td>
</tr>
<tr>
<td><strong>Non-controlling interests</strong></td>
<td>XXX</td>
<td>XXX</td>
<td>XXX</td>
<td></td>
</tr>
<tr>
<td><strong>Total equity</strong></td>
<td>XXX</td>
<td>XXX</td>
<td>XXX</td>
<td>XXX</td>
</tr>
<tr>
<td><strong>Non-current liabilities</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Financial liabilities</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Interest-bearing loans and borrowings</td>
<td>c, q</td>
<td>XXX</td>
<td>XXX</td>
<td>XXX</td>
</tr>
<tr>
<td>Other non-current financial liabilities</td>
<td>e</td>
<td>XXX</td>
<td>XXX</td>
<td>XXX</td>
</tr>
<tr>
<td>Long term provisions</td>
<td></td>
<td>XXX</td>
<td>XXX</td>
<td>XXX</td>
</tr>
<tr>
<td>Government grants</td>
<td>c, d</td>
<td>XXX</td>
<td>XXX</td>
<td>XXX</td>
</tr>
<tr>
<td>Deferred revenue/ Contract liability</td>
<td></td>
<td>XXX</td>
<td>XXX</td>
<td>XXX</td>
</tr>
<tr>
<td>Net employee defined benefit liabilities</td>
<td>i</td>
<td>XXX</td>
<td>XXX</td>
<td>XXX</td>
</tr>
<tr>
<td>Deferred tax liabilities</td>
<td>s</td>
<td>XXX</td>
<td>XXX</td>
<td>XXX</td>
</tr>
<tr>
<td>Other non-current liabilities</td>
<td></td>
<td>XXX</td>
<td>XXX</td>
<td>XXX</td>
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<td></td>
<td></td>
<td></td>
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<td></td>
</tr>
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</table>

Guide to First-time Adoption of Ind AS | 103
<table>
<thead>
<tr>
<th>Footnotes</th>
<th>Local GAAP</th>
<th>Adjustments</th>
<th>(INR million)</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Current liabilities</strong></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Financial liabilities</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Interest-bearing loans and borrowings</td>
<td>n</td>
<td>XXX</td>
<td>XXX</td>
</tr>
<tr>
<td>Trade and other payables</td>
<td>c, d</td>
<td>XXX</td>
<td>XXX</td>
</tr>
<tr>
<td>Other current financial liabilities</td>
<td>e</td>
<td>XXX</td>
<td>XXX</td>
</tr>
<tr>
<td>Government grants</td>
<td></td>
<td>XXX</td>
<td>XXX</td>
</tr>
<tr>
<td>Deferred revenue/ Contract liability</td>
<td>p</td>
<td>XXX</td>
<td>XXX</td>
</tr>
<tr>
<td>Income tax payable</td>
<td></td>
<td>XXX</td>
<td>XXX</td>
</tr>
<tr>
<td>Provisions</td>
<td>o</td>
<td>XXX</td>
<td>XXX</td>
</tr>
<tr>
<td>Liabilities directly associated with the assets classified as held for distribution</td>
<td></td>
<td>XXX</td>
<td>XXX</td>
</tr>
<tr>
<td><strong>Total liabilities</strong></td>
<td></td>
<td>XXX</td>
<td>XXX</td>
</tr>
<tr>
<td><strong>Total equity and liabilities</strong></td>
<td></td>
<td>XXX</td>
<td>XXX</td>
</tr>
</tbody>
</table>

**Assets**

**Non-current assets**

| Property, plant and equipment | c, d, l, m | XXX | XXX | XXX |
| Investment properties | | XXX | XXX | XXX |
| Intangible assets | | XXX | XXX | XXX |
| Investment in an associate/ joint venture | c, d | XXX | XXX | XXX |
| Other non-current financial assets | | XXX | XXX | XXX |
| Deferred tax assets | s | XXX | XXX | XXX |
| **Current assets** | | XXX | XXX | XXX |
| Inventories | c | XXX | XXX | XXX |
| Financial assets | | | | |
| Trade and other receivables | f | XXX | XXX | XXX |
| Other current financial assets | g | XXX | XXX | XXX |
| Cash and short-term deposits | | XXX | XXX | XXX |
| Prepayments | | XXX | XXX | XXX |
| Assets classified as held for distribution | | XXX | XXX | XXX |
| **Total assets** | | XXX | XXX | XXX |
## Group reconciliation of profit or loss for the year ended 31 March 2016

<table>
<thead>
<tr>
<th></th>
<th>Footnotes</th>
<th>Indian GAAP</th>
<th>Adjustments</th>
<th>Ind AS</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Continuing operations</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Sale of goods</td>
<td>c, d</td>
<td>XXX</td>
<td>XXX</td>
<td>XXX</td>
</tr>
<tr>
<td>Rendering of services</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Rental income</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td><strong>Revenue from operations</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Other income</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Finance Income</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td><strong>Total Revenue</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Cost of raw material and components consumed</td>
<td>c, d</td>
<td>XXX</td>
<td>XXX</td>
<td>XXX</td>
</tr>
<tr>
<td>Purchase of traded goods</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>(Increase)/ decrease in inventories of finished goods, work-in-progress and traded goods</td>
<td></td>
<td>XXX</td>
<td>XXX</td>
<td>XXX</td>
</tr>
<tr>
<td><strong>Employee benefits expense</strong></td>
<td>c, d, i,</td>
<td></td>
<td></td>
<td>XXX</td>
</tr>
<tr>
<td>Depreciation and amortization expense</td>
<td>c, d, m</td>
<td></td>
<td></td>
<td>XXX</td>
</tr>
<tr>
<td>Impairment of non-current assets</td>
<td></td>
<td></td>
<td></td>
<td>XXX</td>
</tr>
<tr>
<td>Finance costs</td>
<td>c, d</td>
<td></td>
<td></td>
<td>XXX</td>
</tr>
<tr>
<td>Other expenses</td>
<td>c, d</td>
<td></td>
<td></td>
<td>XXX</td>
</tr>
<tr>
<td>Share of (profit)/ loss from investment in associate and a joint venture</td>
<td>c, d</td>
<td></td>
<td></td>
<td>XXX</td>
</tr>
<tr>
<td><strong>Profit before tax from continuing operations</strong></td>
<td></td>
<td></td>
<td></td>
<td>XXX</td>
</tr>
<tr>
<td>(1) Current tax</td>
<td></td>
<td></td>
<td></td>
<td>XXX</td>
</tr>
<tr>
<td>(2) Adjustment of tax relating to earlier periods</td>
<td></td>
<td></td>
<td></td>
<td>XXX</td>
</tr>
<tr>
<td>(3) Deferred tax</td>
<td>s</td>
<td></td>
<td></td>
<td>XXX</td>
</tr>
<tr>
<td>Income tax expense</td>
<td></td>
<td></td>
<td></td>
<td>XXX</td>
</tr>
<tr>
<td><strong>Profit for the year from continuing operations</strong></td>
<td></td>
<td></td>
<td></td>
<td>XXX</td>
</tr>
</tbody>
</table>

(INR million)
<table>
<thead>
<tr>
<th>Footnotes</th>
<th>Indian GAAP</th>
<th>Adjustments</th>
<th>Ind AS</th>
</tr>
</thead>
<tbody>
<tr>
<td>Profit for the year from continuing operations</td>
<td>XXX</td>
<td>XXX</td>
<td>XXX</td>
</tr>
<tr>
<td><strong>Discontinued Operations</strong></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Profit/(loss) after tax for the year from discontinued operations</td>
<td>XXX</td>
<td>XXX</td>
<td>XXX</td>
</tr>
<tr>
<td>Tax expenses</td>
<td>XXX</td>
<td>XXX</td>
<td>XXX</td>
</tr>
<tr>
<td><strong>Profit/(loss) for the year discontinuing operation</strong></td>
<td>XXX</td>
<td>XXX</td>
<td>XXX</td>
</tr>
<tr>
<td><strong>Profit /(loss) for the year</strong></td>
<td>XXX</td>
<td>XXX</td>
<td>XXX</td>
</tr>
</tbody>
</table>

Attributable to:
- Equity shareholder of parents
- Non-controlling interest

**Other comprehensive income**
*(Other comprehensive income to be reclassified to profit or loss in subsequent period)*

- Exchange differences on translation of foreign operations
- Net movement on cash flow hedges
- Income tax effect
- Net (loss)/gain on available-for-sale financial assets
- Income tax effect
- Actuarial gains and losses on defined benefit plans
- Income tax effect

**Other comprehensive income for the year, net of tax**

**Total comprehensive income for the year, net of tax**

XXX
Footnotes to the reconciliation of equity as at 1 April 2015 and 31 March 2016 and profit or loss for the year ended 31 March 2016

a) Business combinations

The Group has acquired only one business on slump sale basis during the period beginning 1 April 2014 and ending before the transition date. The Group has applied Ind AS 103 to business combinations occurring on or after 1 April 2014. The application of Ind AS 103 resulted in the following changes in carrying amounts of assets and liabilities at the acquisition date:

<table>
<thead>
<tr>
<th>Particulars</th>
<th>Indian GAAP</th>
<th>Adjustment</th>
<th>Ind AS</th>
</tr>
</thead>
<tbody>
<tr>
<td>Land</td>
<td>X</td>
<td>X</td>
<td>X</td>
</tr>
<tr>
<td>Building and Install</td>
<td>X</td>
<td>X</td>
<td>X</td>
</tr>
<tr>
<td>Machine</td>
<td>X</td>
<td>X</td>
<td>X</td>
</tr>
<tr>
<td>Intangible asset</td>
<td>-</td>
<td>X</td>
<td>X</td>
</tr>
<tr>
<td>Inventories</td>
<td>X</td>
<td>(X)</td>
<td>-</td>
</tr>
<tr>
<td>Receivable</td>
<td>X</td>
<td>X</td>
<td>X</td>
</tr>
<tr>
<td>Other Current asset</td>
<td>X</td>
<td>(X)</td>
<td>-</td>
</tr>
<tr>
<td><strong>Total Assets</strong></td>
<td><strong>XXX</strong></td>
<td><strong>XX</strong></td>
<td><strong>XX</strong></td>
</tr>
<tr>
<td>Current liabilities</td>
<td>(XX)</td>
<td>(X)</td>
<td>(XX)</td>
</tr>
<tr>
<td>Deferred income taxes</td>
<td>(XX)</td>
<td>(X)</td>
<td>(XX)</td>
</tr>
<tr>
<td>Contingent liabilities</td>
<td></td>
<td>(X)</td>
<td>(X)</td>
</tr>
<tr>
<td><strong>Total Liabilities</strong></td>
<td><strong>(XX)</strong></td>
<td><strong>(X)</strong></td>
<td><strong>(XX)</strong></td>
</tr>
<tr>
<td>Net Assets</td>
<td>XX</td>
<td>XX</td>
<td>XX</td>
</tr>
<tr>
<td>Enterprise value</td>
<td>XX</td>
<td>XX</td>
<td>XX</td>
</tr>
<tr>
<td>Goodwill</td>
<td>XX</td>
<td>XX</td>
<td>XX</td>
</tr>
</tbody>
</table>

b) Goodwill amortization

Under Indian GAAP, goodwill was amortized on a straight line basis over the economic life of the asset, subject to maximum of 10 years. Under Ind AS, goodwill is not amortized but is measured at cost less impairment losses. For the business combinations restated according to Ind AS 103, the goodwill amortization has been reversed retrospectively. For all other part business combinations, goodwill under Indian GAAP as at the transition date as adjusted for specific adjustments required by Ind AS 101 has been used as carrying amount. After the transition date, no goodwill is amortized; rather, it is tested for impairment annually. The effect of the change is an increase in equity as on 1 April 2015 of INR xxx millions, on 31 March 2016 of INR xxx millions and increase in profit before tax for 31 March 2016 by INR xx millions. The change has no tax effect as deferred taxes are not recognized for temporary difference arising from goodwill for which amortization is not deductible for tax purpose.

The group holds 45% equity interest in ABC Limited. Under Indian GAAP, the Group has treated ABC Limited as its associate and thereby applied equity method of accounting. Under Ind AS, the group has treated ABC Limited as its subsidiary based on *De facto* control and thereby applied line-by-line consolidation. FTA had acquired investment in ABC for INR xxxx million, which is the cost of the subsidiary in FTA’s separate financial statements. The carrying amount of ABC’s net asset on an Ind AS basis will be INR xxxx million. To consolidate ABC at the date of transition, FTA records its investment in its opening Ind AS consolidated balance sheet as follows:

<table>
<thead>
<tr>
<th></th>
<th>Debit</th>
<th>Credit</th>
</tr>
</thead>
<tbody>
<tr>
<td>Various assets and liabilities</td>
<td>xxx</td>
<td></td>
</tr>
<tr>
<td>Goodwill</td>
<td>xxx</td>
<td></td>
</tr>
<tr>
<td>Non-Controlling interest</td>
<td>xx</td>
<td></td>
</tr>
<tr>
<td>Cost of Investment in ABC</td>
<td>xx</td>
<td></td>
</tr>
</tbody>
</table>

The group has tested goodwill for impairment in accordance with Ind AS 36 at the date of transition to Ind AS, regardless of whether there is any indication of impairment. No impairment was deemed necessary at 1 April 2015.
c) Unconsolidated subsidiaries

The group holds 45% equity interest in ABC Limited. Under Indian GAAP, the Group has treated ABC Limited as its associate and thereby applied equity method of accounting. Under Ind AS, the group has treated ABC Limited as its subsidiary based on Defacto control and thereby applied line by line consolidation. FTA had acquired investment in ABC for INR xxxx million, which is the cost of the subsidiary in FTA’s separate financial statements. The carrying amount of ABC’s net asset on an Ind AS basis will be INR xxxx million. To consolidate ABC at the date of transition, FTA records its investment in its opening Ind AS consolidated balance sheet as follows:

<table>
<thead>
<tr>
<th>Assets</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>Goodwill</td>
<td>xxx</td>
</tr>
<tr>
<td>Current Assets</td>
<td>xx</td>
</tr>
<tr>
<td>Trade receivable</td>
<td>xx</td>
</tr>
<tr>
<td>Cash &amp; bank Balance</td>
<td>xx</td>
</tr>
<tr>
<td>Property, plant &amp; equipment</td>
<td>xx</td>
</tr>
<tr>
<td>Loans &amp; advances</td>
<td>xx</td>
</tr>
<tr>
<td>Total Assets</td>
<td>XXXX</td>
</tr>
</tbody>
</table>

The group has tested goodwill for impairment in accordance with Ind AS 36 at the date of transition to Ind AS, regardless of whether there is any indication of impairment. No impairment was deemed necessary at 1 April 2015.

d) Joint venture

The group holds 45% equity interest in ABC Limited. Under Indian GAAP, the Group has treated ABC Limited as its associate and thereby applied equity method of accounting. Under Ind AS, the group has treated ABC Limited as its subsidiary based on Defacto control and thereby applied line by line consolidation. FTA had acquired investment in ABC for INR xxxx million, which is the cost of the subsidiary in FTA’s separate financial statements. The carrying amount of ABC’s net asset on an Ind AS basis will be INR xxxx million. To consolidate ABC at the date of transition, FTA records its investment in its opening Ind AS consolidated balance sheet as follows:

<table>
<thead>
<tr>
<th>Assets</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>Goodwill</td>
<td>xxx</td>
</tr>
<tr>
<td>Current Assets</td>
<td>xx</td>
</tr>
<tr>
<td>Trade receivable</td>
<td>xx</td>
</tr>
<tr>
<td>Cash &amp; bank Balance</td>
<td>xx</td>
</tr>
<tr>
<td>Property, plant &amp; equipment</td>
<td>xx</td>
</tr>
<tr>
<td>Loans &amp; advances</td>
<td>xx</td>
</tr>
<tr>
<td>Total Assets</td>
<td>XXXX</td>
</tr>
</tbody>
</table>

The group has tested goodwill for impairment in accordance with Ind AS 36 at the date of transition to Ind AS, regardless of whether there is any indication of impairment. No impairment was deemed necessary at 1 April 2015.

e) FVTOCI financial assets

The group holds 50% interest in S Limited and exercises joint control over the entity. Under Indian GAAP, the group has proportionately consolidated its interest in the S Limited. On transition to Ind AS, the group has assessed and determined that S Limited is its joint venture under Ind AS 111 Joint Arrangements. Therefore, it needs to be accounted for using the equity method. For the application of equity method, the initial investment is measured as the aggregate of carrying amount of assets and liabilities that the group had previously proportionately consolidated. The carrying amount also includes any goodwill arising on acquisition. The group has tested its investment in joint venture for impairment in accordance with Ind AS 36 at the date of transition to Ind AS. No impairment was deemed necessary at 1 April 2015.

f) Trade and other receivables

Under Indian GAAP, the Group accounted for long term investments in non-quoted and quoted equity shares as investment measured at cost less provision for other than temporary diminution in the value of investments. Under Ind AS, the Group has designated such investments as FVTOCI investments. Ind AS requires FVTOCI investments to be measured at fair value. At the date of transition to Ind AS, difference between the instruments fair value and Indian GAAP carrying amount has been recognized as a separate component of equity, in the FVTOCI equity reserve, net of related deferred taxes.
Under Indian GAAP, the Group accounted for long term investments in debt securities as investment measured at cost less provision for other than temporary diminution in the value of investments. Under Ind AS, the Group has designated certain investments as FVTOCI debt investments. Ind AS requires FVTOCI to be measured at fair value. At the date of transition to Ind AS, difference between instruments’ fair value and Indian GAAP carrying amount has been recognized as a separate component of equity, in the FVTOCI debt reserve, net of related deferred taxes.

g) Other financial assets and liabilities

The fair value of forward foreign exchange contracts is recognized under Ind AS, and was not recognized under Indian GAAP. The contracts, which were designated as hedging instruments under Indian GAAP, have been designated as at the date of transition to Ind AS as hedging instrument in cash flow hedges of either expected future sales for which the group has firm commitments or expected purchases from suppliers that are highly probable. The corresponding adjustment has been recognized as a separate component of equity, in the cash flow hedge reserve.

h) Trade and other payables

Under Indian GAAP, proposed dividends are recognized as a liability in the period to which they relate, irrespective of when they are declared. Under Ind AS, a proposed dividend is recognized as a liability in the period in which it is declared by the company (usually when approved by shareholders in a general meeting) or paid. In the case of Group, declaration of dividend occurs after period end. Therefore, the liability recorded for this dividend has been derecognized against retained earnings.

i) Defined benefit obligation

Both under Indian GAAP and Ind AS, the Group recognized costs related to its post-employment defined benefit plan on an actuarial basis. Under Indian GAAP, the entire cost, including actuarial gains and losses, are charged to profit or loss. Under Ind AS, re-measurements (comprising actuarial gains and losses, the effect of the asset ceiling, excluding amounts included in net interest on the net defined benefit liability and the return on plan assets excluding amounts included in net interest on the net defined benefit liability) are recognized immediately in the balance sheet with a corresponding debit or credit to retained earnings through OCI.

j) Share-based payments

Under Indian GAAP, the Group recognized only the intrinsic value for the long-term incentive plan as an expense. Ind AS requires the fair value of the share options to be determined using an appropriate pricing model recognized over the vesting period. An additional expense of INR xxxx million has been recognized in profit or loss for the year ended 31 March 2016. Share options totalling INRxxxx million, which were granted before and still vesting at 1 April 2015, have been recognized as a separate component of equity against retained earnings at 1 April 2016.

k) Foreign currency translation

Under Indian GAAP, the Group recognized only the intrinsic value for the long-term incentive plan as an expense. Ind AS requires the fair value of the share options to be determined using an appropriate pricing model recognized over the vesting period. An additional expense of INR xxxx millions has been recognized in profit or loss for the year ended 31 March 2016.

l) Property, plant and equipment

The group has elected to measure certain items of property, plant and equipment at fair value at the date of transition to Ind AS. Hence, at the date of transition to Ind AS, an increase of INR xxxx million (31 March 2016: INR xxxx millions) was recognized in property, plant and equipment. This amount has been recognized against retained earnings.

m) Depreciation of property, plant and equipment

Ind AS 16 requires significant component parts of an item of property, plant and equipment to be depreciated separately. The cost of major inspections is capitalized and depreciated separately over the period to the next major inspection. At the date of transition to Ind AS, an increase of INR xxxx million (31 March 2016: INRxxxx million) was recognized in item of property, plant and equipment (note covered in (l) above) net of accumulated depreciation due to separate depreciation of significant components of property, plant and equipment. This amount has been recognized against retained earnings.

n) Interest bearing loans and borrowings

Ind AS 16 requires significant component parts (including major inspections) of an item of property, plant and equipment to be depreciated separately. The cost of major inspections is capitalized and depreciated separately over the period to the next major inspection. At the date of transition to Ind AS, an increase of INR xxxx million (31 March 2016: INRxxxx million) was recognized in item of property, plant and equipment. This amount has been recognized against retained earnings.
AS, an increase of INR xxxx millions (31 March 2016: INR xxxx millions) was recognized in item of property, plant and equipment (note covered in (i) above) net of accumulated depreciation due to separate depreciation of significant components of property, plant and equipment (particularly major inspection). This amount has been recognized against retained earnings.

o) Provisions

Under Indian GAAP, the Group has accounted for provisions, including long-term provision, at the undiscounted amount. In contrast, Ind AS 37 requires that where the effect of time value of money is material, the amount of provision should be the present value of the expenditures expected to be required to settle the obligation. The discount rate(s) should not reflect risks for which future cash flow estimates have been adjusted. Ind AS 37 also provides that where discounting is used, the carrying amount of a provision increases in each period to reflect the passage of time. This increase is recognized as borrowing cost.

p) Deferred revenue/contract liability

Within its electronics segment, the Group operates a loyalty points program, which allows customers to accumulate points when they purchase products in the Group’s retail stores. The points can be redeemed for free products, subject to a minimum number of points being obtained. Under Indian GAAP, the Group creates a provision toward its liability under the reward program.

Under Ind AS, consideration received is allocated between the electronic products sold and the points issued on a relative stand-alone selling price basis. If the stand-alone selling price for a customer’s option to acquire additional goods or services is not directly observable, the group estimates it. Fair value of the points is determined by applying a statistical analysis. The fair value allocated to the points issued is deferred and recognized as revenue when the points are redeemed.

q) Convertible preference shares

The group has issued convertible redeemable preference shares. The preference shares carry fixed cumulative dividend, which is non-discretionary. Under Indian GAAP, the preference shares were classified as equity and dividend payable thereon was treated as distribution of profit.

Under Ind AS, convertible preference shares are separated into liability and equity components based on the terms of the contract. Interest on liability component is recognised using the effective interest method.

r) Government grant

The Group has received an interest-free loan under the development scheme from the government for INR xxx million. Under the Indian GAAP, the Group has accounted for the loan as liability and the carrying amount was INR xxx million at the date of transition to Ind AS. The Group will apply Ind AS 109 to the measurement of such loan after 1 April 2015 (date of Transition to Ind AS). Since the loan does not carry any interest and is repayable at the amount recognized in the opening balance sheet, no interest needs to be recognized on the loan.

s) Deferred tax

Indian GAAP requires deferred tax accounting using the income statement approach, which focuses on differences between taxable profits and accounting profits for the period. Ind AS 12 requires entities to account for deferred taxes using the balance sheet approach, which focuses on temporary differences between the carrying amount of an asset or liability in the balance sheet and its tax base. The application of Ind AS 12 approach has resulted in recognition of deferred tax on new temporary differences, which was not required under Indian GAAP.

In addition, the various transitional adjustments lead to different temporary differences. According to the accounting policies, the Group has to account for such differences. Deferred tax adjustments are recognized in correlation to the underlying transaction either in retained earnings or a separate component of equity.

t) Other comprehensive income

Under Indian GAAP, the Group has not presented other comprehensive income (OCI) separately. Hence, it has reconciled Indian GAAP profit or loss to profit or loss according to Ind AS. Furthermore, Ind AS profit or loss is reconciled to total comprehensive income as per Ind AS.

u) Statement of cash flows

The transition from Indian GAAP to Ind AS has not had a material impact on the statement of cash flows.

v) Errors under Indian GAAP

If errors made under Indian GAAP are discovered during the transition to Ind AS, any adjustments to equity or comprehensive income for these amounts must be identified as error corrections in the reconciliation rather than as Ind AS transition adjustments. As part of transition process, the Group has not discovered any errors under the Indian GAAP.
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EYN1506-069
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