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Ind AS 103:
Business Combinations

Indian Accounting Standards
Practical Learning Class
Gearing up to speak the new accounting language

Contents

Overview

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Objective	To improve the relevance, reliability and comparability of the information provided in financial statements about a business combination and its effects
Scope	**Does not apply to:** • formation of a joint venture • acquisition of an asset or asset group that is not 'a business' • combination of entities or businesses under common control

Definition - Business

Business

An integrated set of activities and assets capable of being conducted and managed for the purpose of providing a return in form of dividends, lower costs or other economic benefits directly to investors, other owners, members, or participants

- **outputs are not required** for an integrated set to qualify as a business
- it is **not relevant** whether the **seller previously operated the set as a**
- **business** or **whether the acquirer intends to operate as a business**
- a set **can be considered** a business when it does not contain all the assets and activities that the seller used in operating that business, **so long as market participants are capable of acquiring or otherwise providing the missing elements**.

Business – Example 1

Example

Company A acquires entity B. B's only activity is to hold and administer investment property assets. Is the acquisition a business combination or the purchase of an asset when:

Situation 1: B holds a single investment property with no tenants, no staff and does not undertake any services

Situation 2: B holds a single investment property with tenants and undertakes servicing the existing tenants (rent collection, routine maintenance, etc.)

Solution

Situation 1 Asset purchase – outside the scope of Ind AS 103

Situation 2: Judgment required, but probably an asset purchase

Business – Example 2

Example:

Company S is a manufacturer company. Its payroll and accounting system is managed as a separate cost centre, which supports all the operating segments and the head office functions.
Company A agrees to acquire the assets, liabilities and workforce of the operating segments of Company S but does not acquire the payroll and accounting cost centre or any head office functions.

Does A need to apply the provisions of Ind AS 103

Solution:

The acquisition is a business combination as activities and assets of operating segments are capable of being managed as a business.

Payroll and accounting cost centre are not used to create outputs and are generally not considered an essential element in the assessment of business.

Business Combinations – Step by step

- step 1: identify a business combination
- step 2: identify the acquirer
- step 3: determine the acquisition date
- step 4: recognise/measure identifiable assets acquired/liabilities assumed
- step 5: recognise/measure any non-controlling interest
- step 6: determine the consideration transferred
- step 7: recognise/measure goodwill (or gain from a bargain purchase)

Business Combination

Business combination

A transaction or other event in which an acquirer obtains control of one or more businesses.

Control

An investor controls an investee if and only if the investor has all the following:

- power over the investee
- exposure, or rights, to variable returns from its involvement with the investee; and
- the ability to use its power over the investee to affect the amount of the investor's returns.

If the transaction/ assets acquired are not a business, the reporting entity shall account for the transaction or other event as an asset acquisition

Business combination v/s Asset purchase

Topic	Business combination	Asset acquisition
Accounting	Accounted for using the acquisition method	Recognise assets and liabilities by allocating the cost on the basis of their relative fair values
Goodwill	Gives rise to goodwill or a gain on bargain purchase	Does not give rise to goodwill
Transaction costs	Expensed when incurred	Typically capitalised
Deferred tax on initial temporary differences	Recognised as assets and liabilities	Not recognised unless specific circumstances apply
Contingent consideration	Recognised and measured at FV on the acquisition date	No specific guidance in Ind AS

Common control

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Common control
A business combination in which all of the combining entities or businesses are **ultimately** controlled by **the same party or parties both before and after** the business combination, and that control is **not transitory**.

Additional guidance is given in Ind AS 103 regarding accounting for business combinations under Common control

Accounting of common control transactions :

- assets and liabilities are recorded at **book value**
- **any expenses** of the combination are **written off immediately** in the P&L
- **comparative amounts are restated** as if the combination had taken place at the beginning of the earliest comparative period presented
- adjustment are allowed only to harmonise accounting policies, no other adjustment allowed
- consideration to be recorded as follows: Securities – at nominal value and asset other than cash – at fair value
- balance of retained earning – to be aggregated with transferee or to be transferred to general reserve

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Identifying the acquirer

Factor to consider	Who is *usually* the acquirer?
combination effected primarily by transferring cash or other assets or by incurring liabilities	the entity that transfers the cash or other assets or incurs the liabilities.
Combination effected primarily by exchanging equity interests	the entity that issues the equity interests
Relative voting rights in the combined entity	the entity whose owners as a group retain or receive the largest portion of the voting rights in the combined entity
Composition of the governing body of the combined entity	the entity whose owners have the ability to elect or appoint or remove a majority of the members of the governing body of the combined entity
Relative size	the entity whose size is significantly greater than that of the other combining entity or entities
More than two entities involved	the entity that initiated the combination
A new entity is formed to effect a new business combination	if the entity is formed to issue equity instruments, one of the existing combining entities is the acquirer where if the new entity transfers cash (or other assets or incurs liabilities) the new entity may be the acquirer

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Acquisition date

Acquisition date

The date on which the acquirer **obtains control** of the acquiree

The date from which:

- the acquirer **recognises & measures** the **consideration**, **assets acquired** and **liabilities assumed**
- the acquiree's results are **consolidated** from that day forward

For e.g. Company A and Company B begin negotiations on 30 June 2014 for Company A to acquire Company B. The entities finalise the sale & purchase agreement (SPA) on 1 November 2014. However, the SPA states that control is transferred from 31 December 2014. What is the acquisition date in this case?

Solution: Judgment is required to analyse whether the effective date provision in the SPA actually changes the acquisition date. However, this may not change the date when the control is transferred.

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Recognition and measurement

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Measurement

Assets acquired and liabilities assumed are **recognised** at fair value if:

- **meet the definition** of an asset or liability at the acquisition date
- are **part of exchange** in the business combination

Classification

The **acquirer classifies and designates** assets and liabilities at **acquisition date** based on:

- acquirer's economic conditions
- contractual terms of the assets/liabilities
- acquirer's operating or accounting policies

Acquirer's classification/designations may differ from those of the acquiree

Exception to the classification

Leases are classified based on contractual terms and other factors as determined at the inception of lease contract and not on the acquisition date

Recognition : Exceptions

Contingent liabilities

Ind AS 37

- a **contingent liability** is…a **present obligation** that arises from past events but is **not recognised** because: (i) it is **not probable**…or (ii) the **amount** of the obligation **cannot be measured** with sufficient **reliability**

Ind AS 103

- recognised only if a **present obligation** exists **and fair value can be measured reliably**
- recognised **even if** an outflow of economic benefits is **not probable** (uncertainty is considered in the determination of fair value)

Measurement: Exceptions

Reacquired rights

recognition

- recognise an intangible asset if it reacquires a right it had previously granted to the acquiree to use the acquirer's recognised / unrecognised assets

initial measurement

- on the basis of the remaining term of the related contract without attributing value to possible renewals
- if terms of the contract that gives rise to the reacquired right are either favourable/unfavourable compared to current market terms, acquirer recognised a gain/loss on the acquisition date separately from the business combination

subsequent measurement

- amortised over the remaining contractual period

Reacquired Rights: Example 3

Example:

Company Q granted a 5-year license to Company S to use Company Q's technology at a fixed annual fee. S is able to cancel the license agreement by paying a fee of INR 2 million. Two years into the agreement, Q acquires S for INR 100 million. On that date, the fair value of the license agreement is INR 4.5 million (includes INR 0.5 million relating to the value of expected renewals). The terms of the license agreement are unfavourable to Company Q when compared to market terms by INR 1.5 million.

Solution

- settlement loss = INR 1.5 million (lower of the value of the unfavourable pricing (INR 1.5 million) and the contractual termination fee (INR 2 million))
- consideration transferred = INR 98.5 million
  (representing the contractual price of INR100 million – INR 1.5 million loss)
- initial measurement for reacquired right = INR 4 million
- (INR 4.5 million fair value – INR 0.5 million expected renewals)

Recognition and measurement: Exceptions
Indemnification assets

recognition

- at the same time it recognises the indemnified item

initial measurement

- on the same basis as the indemnified item (subject to the need for a valuation allowance for uncollectible amounts)

subsequent measurement

- on the same basis as the indemnified liability or asset, subject to contractual limitations on amount
- for those not measured at FV, management's assessment of collectability of the indemnification asset

derecognition

- when the entity collects the asset, sells it or otherwise loses the right to it

Recognition and measurement

Intangible assets

Is the asset identifiable?

does the asset meet the **contractual-legal criterion**

does the asset meet the **separability** criterion

Yes

Yes

is the entity **prohibited** from transferring/exchanging the information

No

recognise, separately from goodwill, the **identifiable intangible assets** acquired

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Recognising and measuring any non-controlling interest (NCI)

non-controlling interest: the equity in a subsidiary not attributable, directly or indirectly, to a parent

Category	Description	Example	Measurement option?
present ownership instrument	acquiree's shares held by non-selling shareholders that entitle them to a proportionate share of the acquiree's net assets in the event of liquidation	common or ordinary shares	yes - fair value or proportionate share of recognised assets and liabilities
other components of NCI	other financial instruments issued by the acquiree that meet Ind AS 32's definition of equity	warrants or call options (on fixed-for-fixed terms)	no - fair value

Recognising and measuring: NCI –Example 4

Fair value model vs. proportionate interest model

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Company A pays INR 800 for an 80% interest in Company B. Company A does not have any previously held equity interest in Company B. The fair value of Company B's identifiable net assets is estimated to be INR 750. Using a valuation technique, the fair value of the remaining 20% in Company B (the NCI) on the acquisition date is determined to be INR 180.

	FV Model	% Interest
Cash consideration	800	800
NCI at fair value	180	-
NCI at 20% of identifiable net assets	-	150
Total	980	950
Fair value of 100% of identifiable net assets	750	750
Goodwill	**230**	**200**
Recognised amount of NCI	**180**	**150**

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Determine the consideration transferred

consideration transferred is the sum of the acquisition-date fair values of:

- the **assets transferred** by the acquirer
- the **liabilities incurred** by the acquirer to former owners of the target company and
- **equity interests issued** by the acquirer

in exchange for the acquiree

(**includes** contingent consideration)

(**excludes** acquisition costs)

Determine the consideration transferred

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transferred assets / liabilities carrying amount differ from fair value

remain within the combined entity after business combination?
(eg transferred to acquiree rather than former owners)

N	Y
• remeasure to fair value at acquisition date • recognise gain or loss in p/l	• measure at carrying amounts immediately before acquisition date • do not recognise gain or loss in p/l (if controlled both before and after the combination)

Determine the consideration transferred

Contingent consideration

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contingent consideration: an obligation of the acquirer to transfer additional assets or equity interest to the acquiree's former owners if specified future events occur or conditions are met

recognised and measured at fair value on the acquisition date

- directly impacts goodwill and reported liabilities or equity

apply Ind AS 32 to determine classification as financial liability or equity

- liability subsequently remeasured (FVTPL) until settled
- equity not remeasured

Determine the consideration transferred: Example 5

Contingent consideration

Example:

An acquirer purchased a business in the pharmaceutical industry. The sale and purchase agreement specifies the amount payable as:

- cash of INR 100 million to be paid on the acquisition date
- an additional 1,000,000 shares of the acquirer to be paid after 2 years if a specified drug receives regulatory approval.

What is the consideration transferred and how should it be accounted for?

Consideration transferred =

- cash paid (INR 100 million) +
- fair value of 1,000,000 shares in 2 years' time (contingent consideration).
  - fair value of the contingent consideration would be based on a 2-year forward price, reduced by the effect of the performance conditions
  - classification based on definition in Ind AS 32 (only settled by issuing fixed number of shares or 'fixed for fixed' = equity)
    - no subsequent adjustment for changes in fair value of shares

Determine the consideration transferred

contractual purchase price (based on the SPA) + or − **adjustments for transactions not part of the business combination** = **consideration transferred in exchange for the acquiree**

- remuneration for employees or former owners for future services
- reimbursement of the acquiree or former owners for paying the acquirer's acquisition-related costs
- settlement of pre-existing relationships
- replacement of acquiree share-based payment awards
- contracts to acquire shares from non-selling shareholders

Settlement of a pre-existing relationship

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Y

settles a pre-existing relationship?

acquirer recognises gain or loss equal to =

for non-contractual relationship

fair value

for contractual relationship = lesser of:

amount by which contract is favourable or unfavourable from perspective of acquirer when compared to terms for current market transactions

A

the amount of any stated settlement provisions in the contract available to the counterparty to whom the contract is unfavourable

B

Arrangements for contingent payments to employees or selling shareholders

Whether arrangements for contingent payments to employees or selling shareholders are

- **contingent consideration** in the business combination or
- **separate transactions**

depends on the nature of the arrangements

Following indicators are to be considered if it is not clear whether an arrangement

Indicators	
Continuing employment	Number of shares owned
Duration of continuing employment	Linkage to the valuation
Level of remuneration	Formula for determining consideration
Incremental payments to employees	Other agreements and issues

Replacement of acquiree share-based payment awards

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acquirer's SBP awards

Acquirer

Acquiree

acquiree's existing SBP awards

objective is to **allocate the replacement award's value** between the amounts attributable to :

- **pre-combination service** (treated as part of **consideration transferred**)
- **post-combination service** (accounted for as **compensation expense** in the post combination financial statements)

Contracts to acquire shares from non-selling shareholders

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purchased call options → written put options → forward contracts

in substance, is the contract in question an **arrangement to purchase** additional acquiree shares **at a future date**?

Ind AS 103's indicators on identifying separate transactions

Ind AS 110

in substance, is the contract in question a **purchase** of the underlying acquiree shares **for a deferred or contingent consideration**?

(not transferred)
accounted for **separately** from the business combination

(transferred)
forms **part of the business combination** transaction

Accounted for as per relevant accounting standard

Accounted for as per Ind AS 103

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Goodwill / Gain on bargain purchase calculation

consideration transferred

\+ **plus** amount of NCI

\+ **plus** FV of previously held equity interest

− **less** net of assets acquired and liabilities assumed

= **equals** goodwill (or gain on bargain purchase)

Goodwill or gain from a bargain purchase

Result	Ind AS 103 treatment
goodwill	• recognised as a **separate asset** in the acquirer's consolidated financial statements • goodwill is **not amortised** but is subject to at least an **annual impairment test**
gain from a bargain purchase	• double check accounting • recognised in OCI **(In IFRS 3 recognized in profit or loss immediately)**

Business combination achieved in stages

acquirer remeasures its previously held equity interest in the acquiree at its acquisition-date fair value

in prior periods, did the acquirer recognise changes in the value of the equity interest in OCI?

Y

amount that was recognised in OCI should be recognised on the same basis as would be required if the acquirer had disposed directly of the previously held equity interest

N

any resulting gain or loss recognised in profit or loss

Case study 1

See case study 1: Recognising and measuring goodwill or a gain from bargain purchase – step acquisition

Case study 1 debrief

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A's consolidated financial statements	INR	INR
dr. identifiable net assets of Entity B*	2,100,000	
dr. goodwill	400,000	
dr. reclassification of gain on previously held interest in Entity B from OCI	150,000	
cr. cash		2,250,000
cr. available for sale investment in Entity B		250,000
cr. reclassification of gain on previously held interest in Entity B to profit and loss		150,000

Measurement period

Initial accounting incomplete at the reporting date

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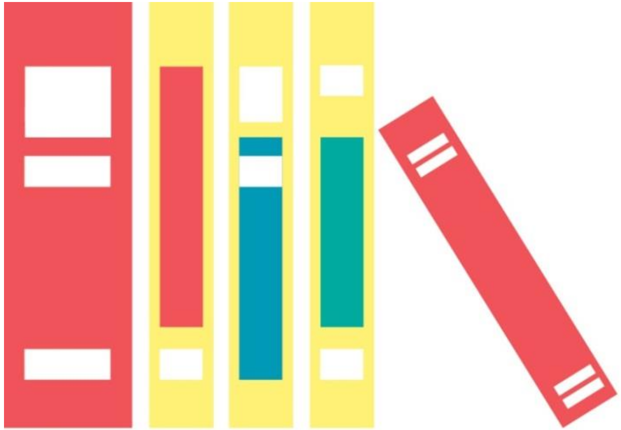
Measurement period adjustments	Other adjustments during measurement period	Post-measurement period adjustments
• **limited** to those that arise from new information obtained about facts and circumstances that existed **at the acquisition date** **Accounting:** • retrospectively adjust the provisional amounts and/or recognise new assets/liabilities to reflect the new information • **adjust goodwill**	• include adjustments for **developments after the acquisition date** but during the measurement period (eg changes in estimates) **Accounting:** • **prospectively adjust provisional amounts** to reflect new information arising after the acquisition date • **no adjustment to goodwill** • correct errors retrospectively in accordance with Ind AS 8	**Accounting:** • **no adjustment to the accounting for the business combination** allowed except for the correction of an error in accordance with Ind AS 8

Thank you!



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Group accounting: Consolidation, joint arrangements and disclosures

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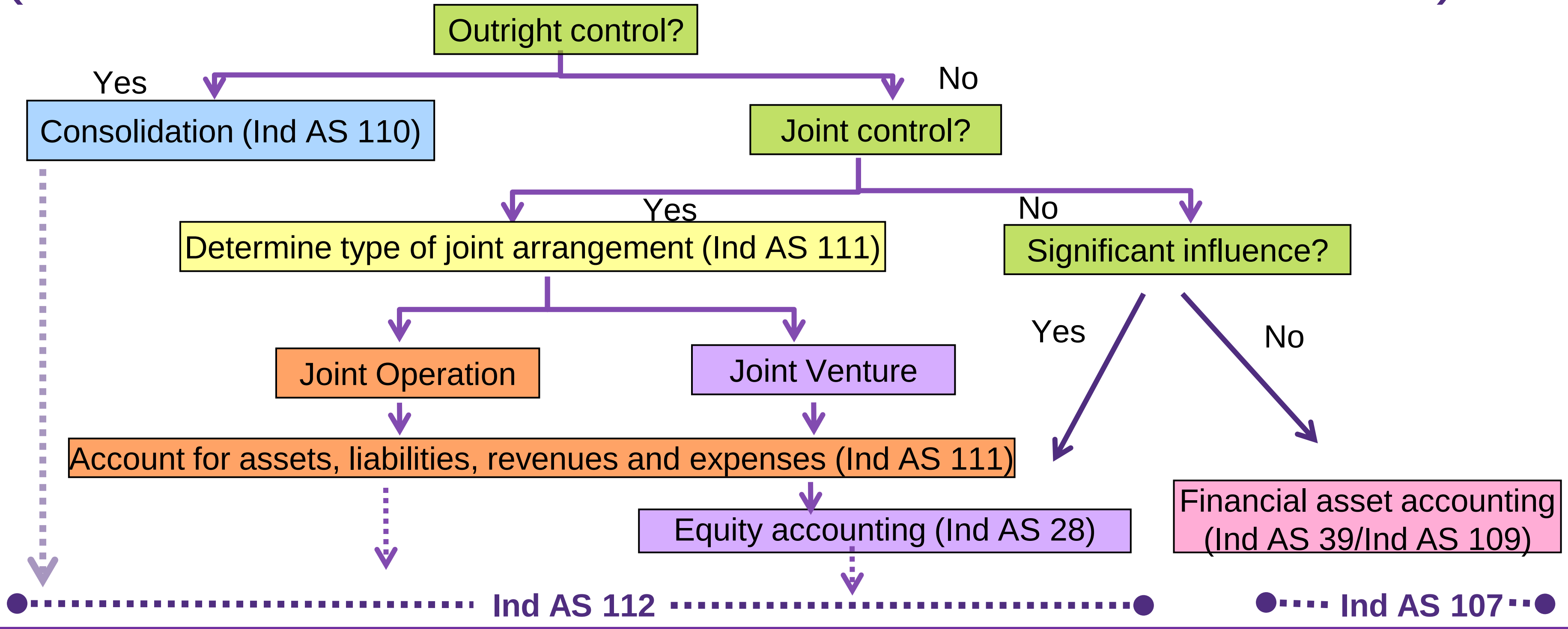
Contents

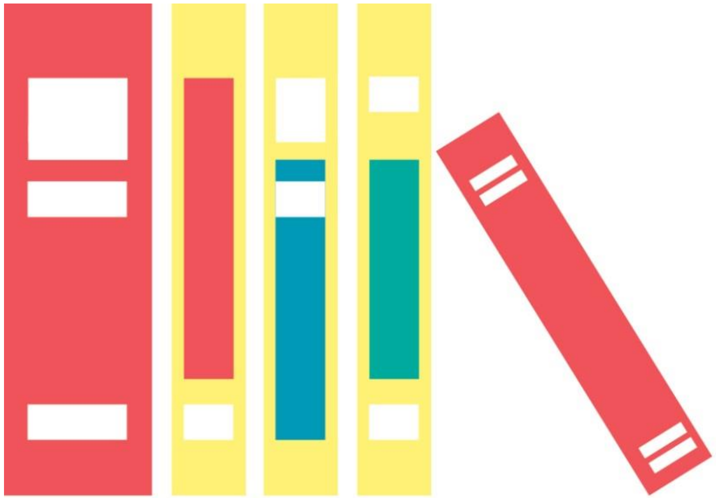
1. Ind AS 110 Consolidated Financial Statements
2. Investment entities
3. Ind AS 111 Joint Arrangements
4. Ind AS 112 Disclosures of Interests in Other Entities

Determining the accounting for interests in other entities

(Interaction of Ind AS 110, 111, 112 and Ind AS 28)



Ind AS 110: Consolidated Financial Statements



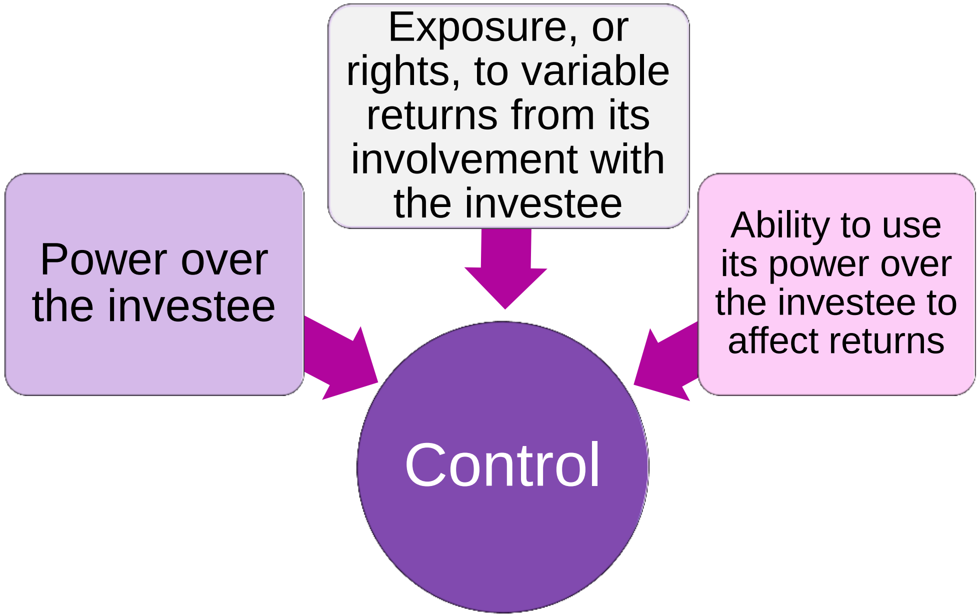
Ind AS 110 – scope and scope exceptions

An entity that is parent shall present consolidated financial statement. Consolidated financial statement applies to all entities, except as follows:

- An intermediate parent under the following conditions:
  - it is a wholly-owned subsidiary or is a partially-owned subsidiary of another entity and all its other owners, have been informed about it, and do not object
  - its debt or equity instruments are not traded in a public market
  - it did not file, nor is it in the process of filing, its financial statements with a regulatory organisation for issuing any instruments in a public market; and
  - its ultimate or any intermediate parent produces consolidated financial statements that are available for public use and comply with Ind ASs

- Post-employment benefit plans or other long-term employee benefit plans to which Ind AS 19 Employee Benefits applies
- Investment entities

The definition of control



All three elements of control **must** be present to conclude that an investor controls an investee

Applying the control model - focus on 'power'

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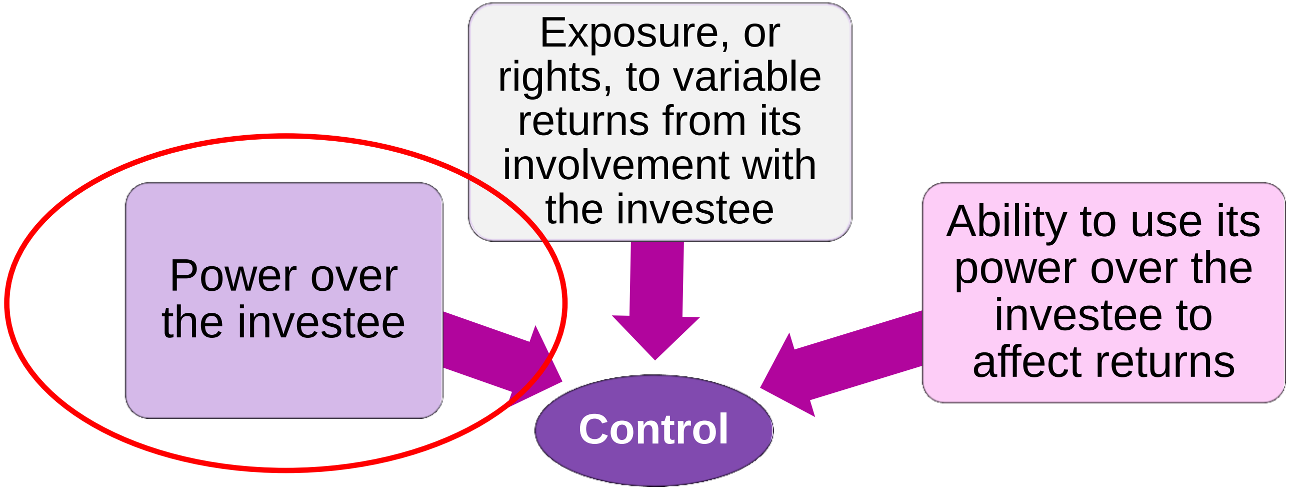


Power = **Existing rights** that give the **current ability** to direct the **relevant activities**

Current ability does not necessarily require the rights to be exercisable immediately. Instead, the key factor is whether the rights can be exercised before decisions about relevant activities need to be taken.

Identifying relevant activities

Who appoints the Board and key management personnel?

Who can change the strategic direction of the entity?

Relevant activities are those activities that **significantly** affect the **investee's return.**

Group question

Q:

Investor A holds 48% of the voting rights of an investee (Investee B). The remaining voting rights are held by thousands of other shareholders, none individually holding more than 1% of the voting rights. None of the shareholders has any arrangements to consult with any other shareholders or make collective decisions. Relevant activities are directed by a simple majority vote.

Is the information provided enough to conclude Investor A has power over Investee B or should A consider other facts and circumstances?

A:

In this case, on the basis of the absolute size of its holding and the relative size of the other shareholdings, the investor may conclude that it has a sufficiently dominant voting interest to meet the power criterion without the need to consider any other evidence of power.

While other facts and circumstances should or may always be considered; in this case, other facts and circumstances (including voting behaviour of other shareholders) is unnecessary, but not precluded.

Rights that can give an investor power over an investee

- **Voting rights**
- **Potential voting rights**
- **Rights to appoint/remove KMP/Board**
- **Rights to enter into/veto transactions**
- **Other rights**

To have **power** over an investee, an investor must have **existing rights** that give it the **current ability** to direct the **relevant activities**.

Case study 1

See case study 1: Rights to direct different relevant activities

Substantive vs. protective rights

Substantive

- **practical ability to exercise** that right
- right **exercisable when decisions** impacting relevant activities must be **made**

Protective*

- designed to **protect** the interest of the holder
- **without** giving holder **power** over the entity to which they relate

***** Examples of protective rights:

- Prevent from undertaking activities that could significantly change the credit risk
- Blocking rights over matters such as foreign takeover

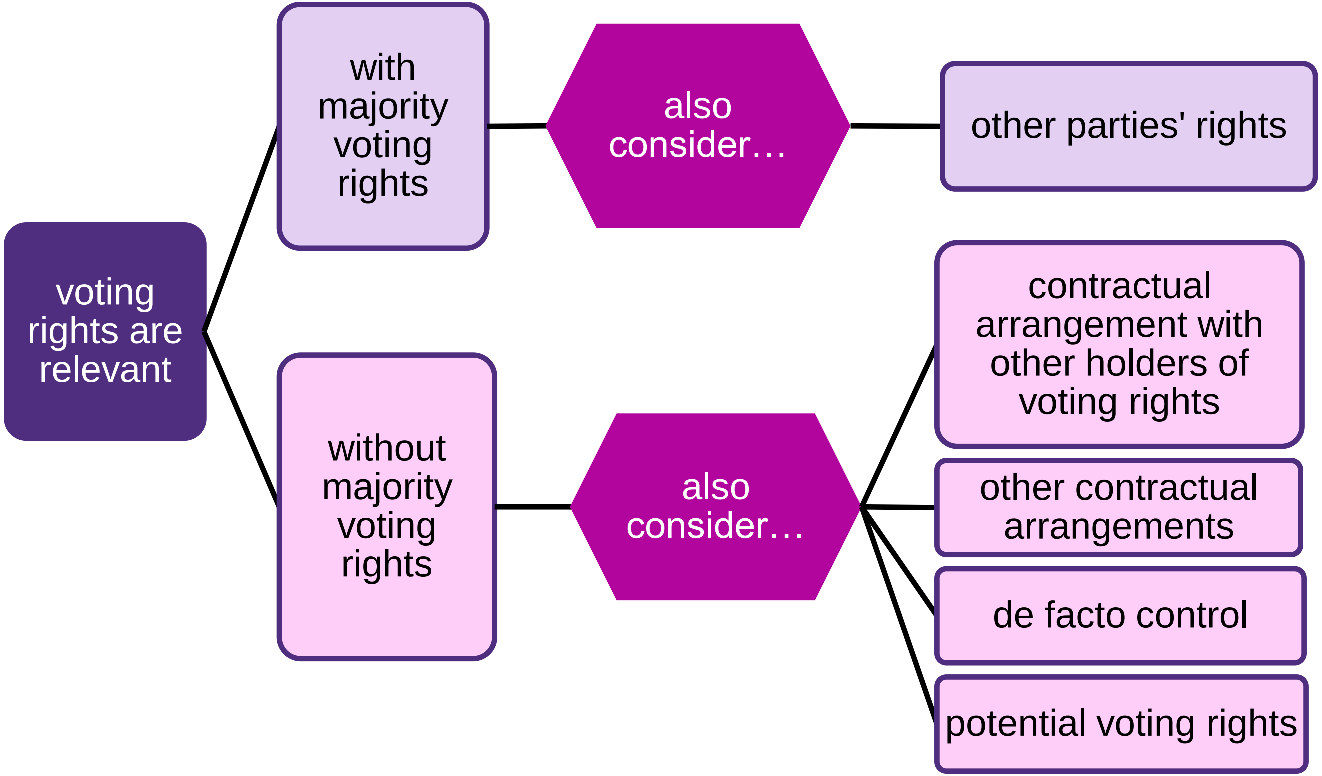
Substantive vs. protective rights

Type of rights held by investor	Type of rights held by other parties	Does the investor have control
Substantive	Protective	Yes
Protective	Substantive	No
Substantive	Substantive	Further analysis required

Case study 2

See case study 2: Substantive vs. protective rights

Voting rights



De facto control
(In reality, actually, from the fact)

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Investor with less than a majority of voting rights may have defacto control

More likely that investor has control of investee

Increasing size/number

--- Indicators ---

- Number of voting rights held by investor
- Size of investor's holding of voting rights relative to other vote-holders
- Number of other parties that would have to act together to outvote investor

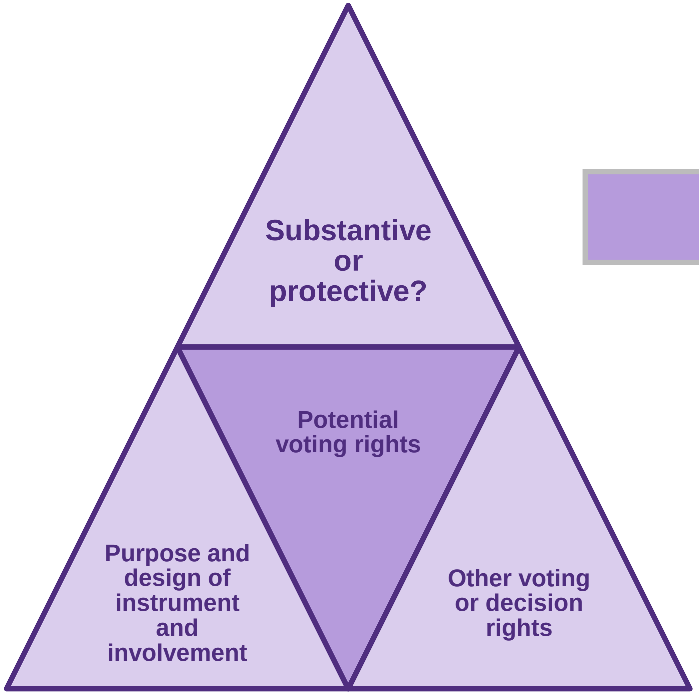
Decreasing size/number

Less likely that investor has control of investee

Case studies 3, 4, 5

See case studies 3, 4, 5: Power without majority of voting rights

Potential voting rights



- Practical ability to exercise
  - (in/out of money options)
- Non-currently exercisable rights

Rights to **obtain** voting rights of an investee

Case study 6

See case study 6: Potential voting rights

Applying the control model -- exposure or rights to variable returns

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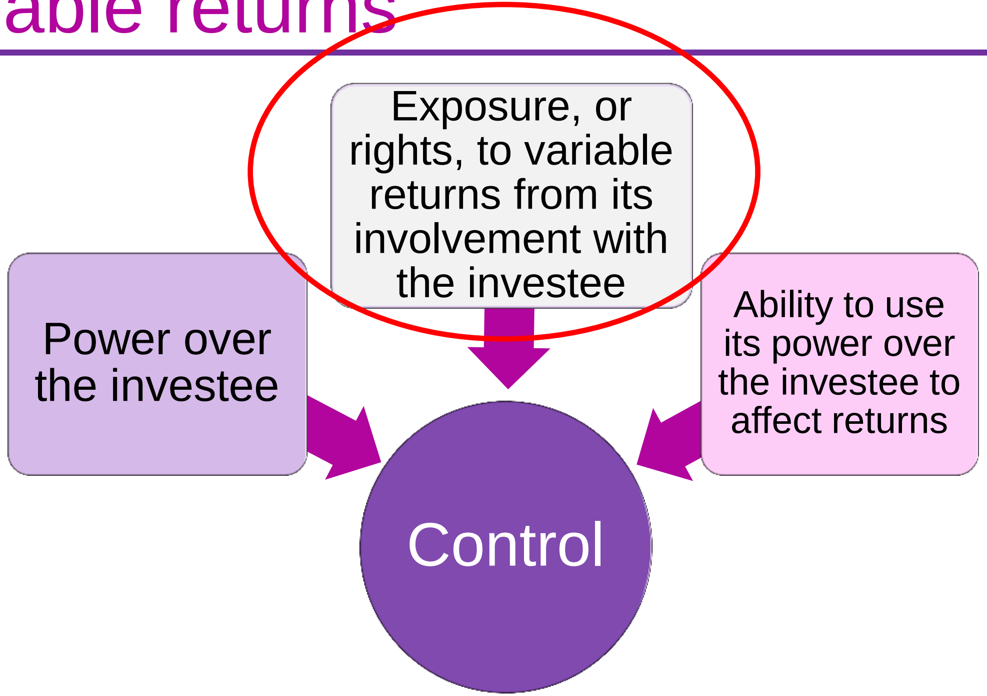

All **three** elements of control **must** be present to conclude that an investor controls an investee.

Variable returns

Variable returns are **returns** that are **not fixed** and have the potential to vary as a **result** of the performance of an **investee**. Variable returns can be **only positive**, **only negative** or both **positive and negative.**

'returns' not 'benefits'…think broadly

existence vs amount

look again! substance over form

Applying the control model -- ability to use its power over the investee to affect returns

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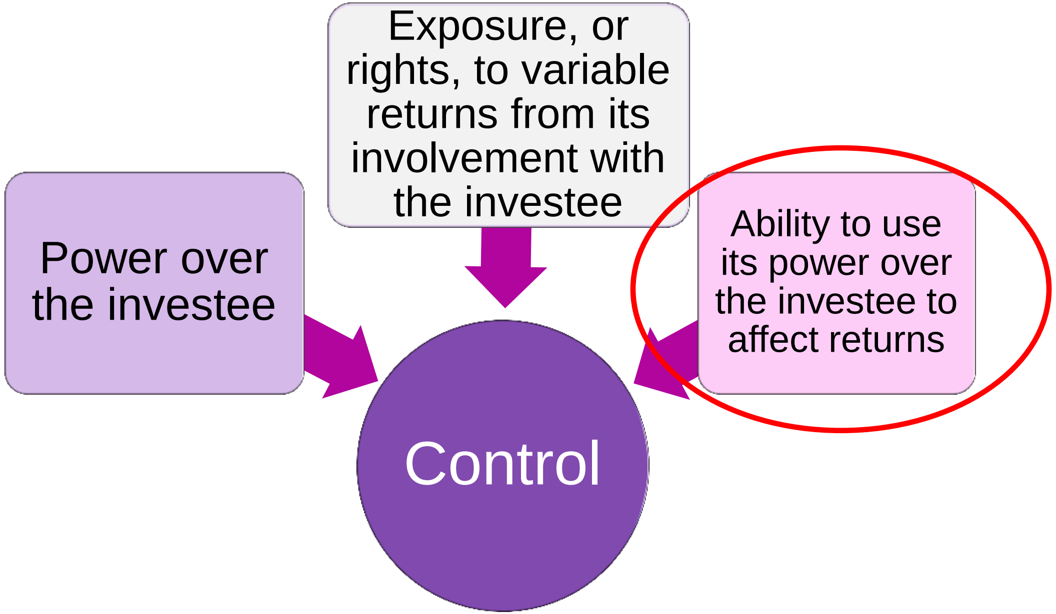

Principal vs. agent considerations

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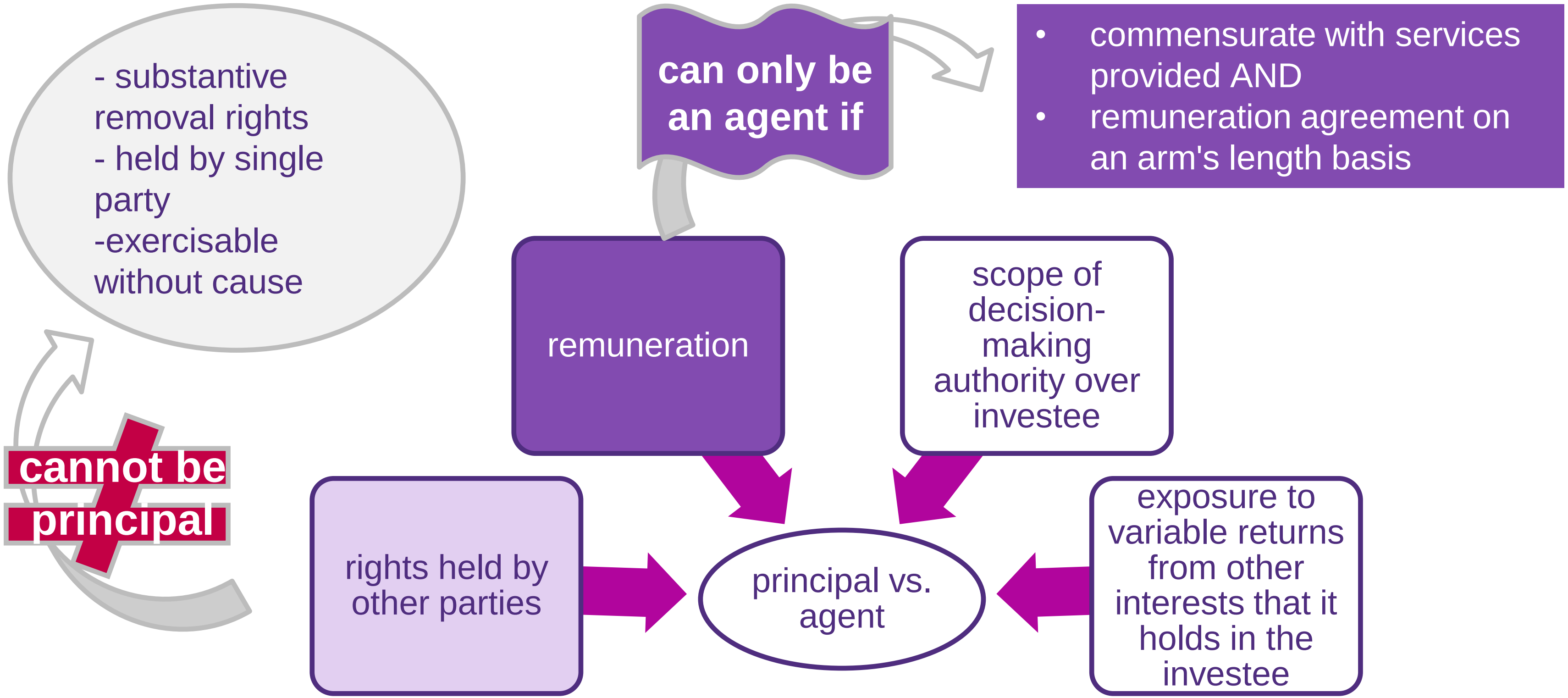
- remuneration
- scope of decision-making authority over investee
- rights held by other parties
- exposure to variable returns from other interests that it holds in the investee

→ principal vs. agent

An **agent** is a party primarily engaged to act on behalf of and for the benefit of another party or parties (the principal(s)) and therefore does not control the investee when it exercises its decision-making authority.

Principal vs. agent



Accounting requirements

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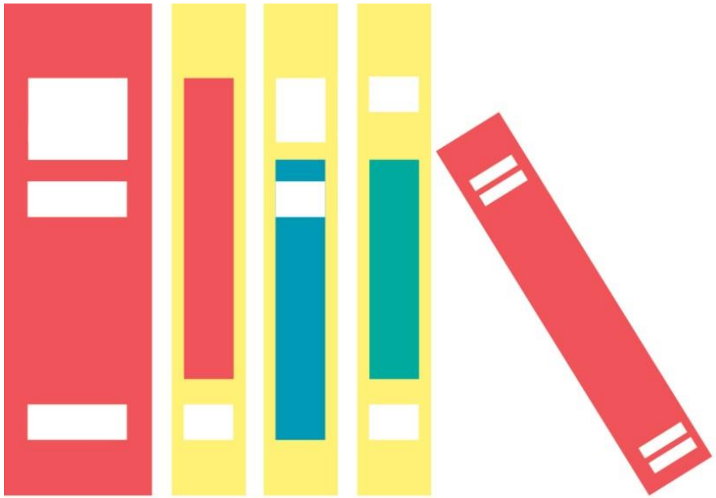
Consolidation procedures	• Line by line addition, intercompany elimination, translation of foreign operations
Uniform accounting policies	• Accounting policies of all entities consolidated need to be harmonised
Profit / loss allocation	• Profit/loss allocation is between controlling and non-controlling interest is based on actual share ownership
Non-controlling interest (NCI)	• NCI is shown separately within equity • Loss is allocated even if NCI balance is negative
Loss of control	• Gain/loss arising on loss of control is recognised in income statement • No P&L impact where no loss of control

Consolidation - Investment Entities



Defining an investment entity
Figure 11

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does the entity meet all three elements of the investment entity definition:

- investment services condition
- business purpose condition
- fair value condition

Y → investment entity

N → not an investment entity

also consider

does the entity have all four 'typical characteristics' of an investment entity

- multiple investments
- multiple investors
- investors that are not related parties
- ownership interests in form of equity or similar interests?

N → apply more judgement to assess if definition met

Defining an investment entity continued…

investment services	• obtains funds from one or more investors and provides those investor(s) with investment management services • question of fact
business purpose	• invests funds solely for returns from capital appreciation, investment income or both • evidenced in underlying documents or marketing materials • exit strategy • no special benefits from investees
fair value*	• reports fair value to investors and KMP • KMP use fair value as the primary measure of performance to make investment decisions • measures substantially all investments using fair value

* Investment property is to be measured at cost under Ind AS. Hence Ind AS has been amended by exposure draft dated Dec 13, 2013

Case study 7

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See case study 7: Permitted and prohibited activities

Accounting requirements for investment entities

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subsidiaries held as investments

- measured at FVTPL
- Ind AS 103 does not apply
- exemption applies to controlling interests in another investment entity

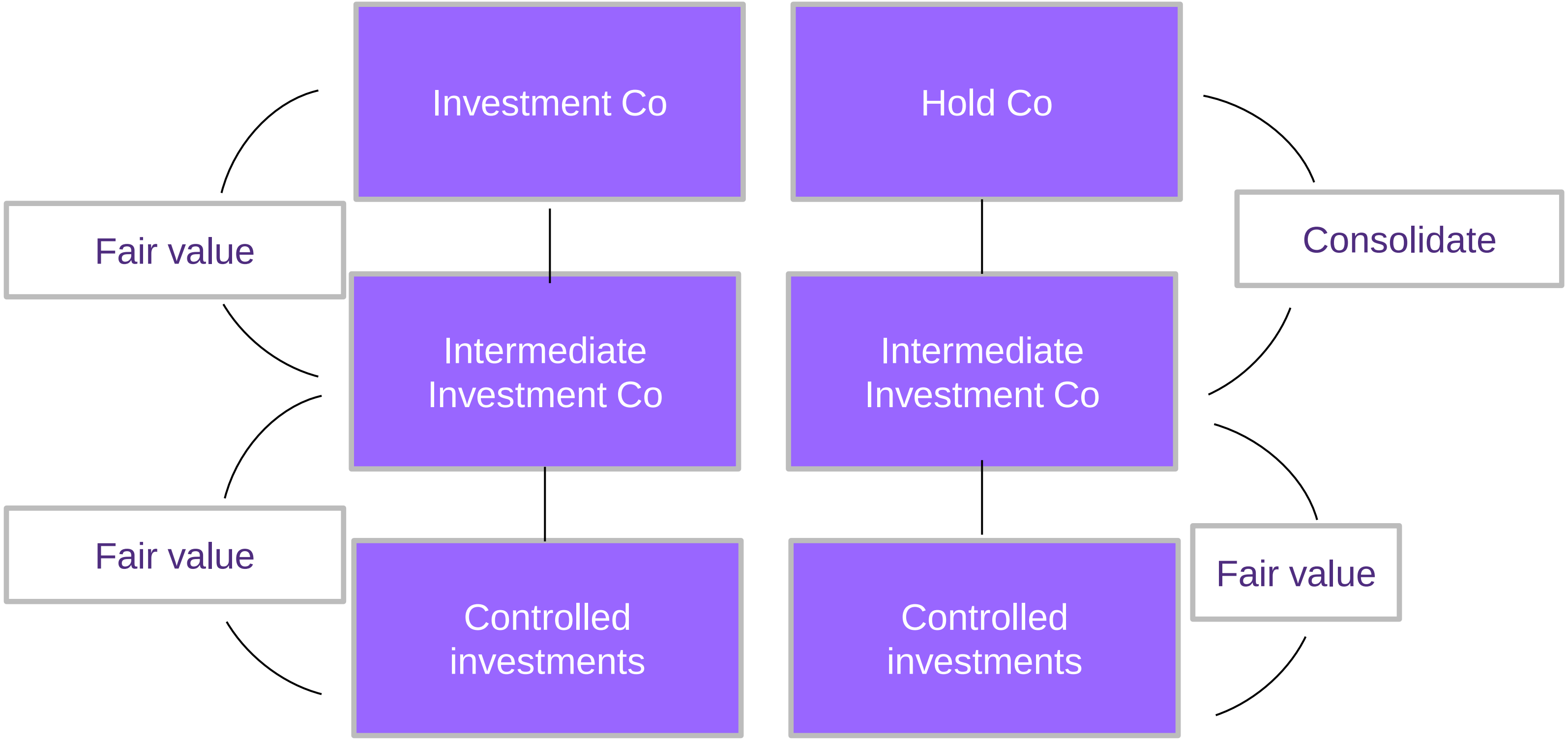
service subsidiaries

- consolidate
- Ind AS 103 applies

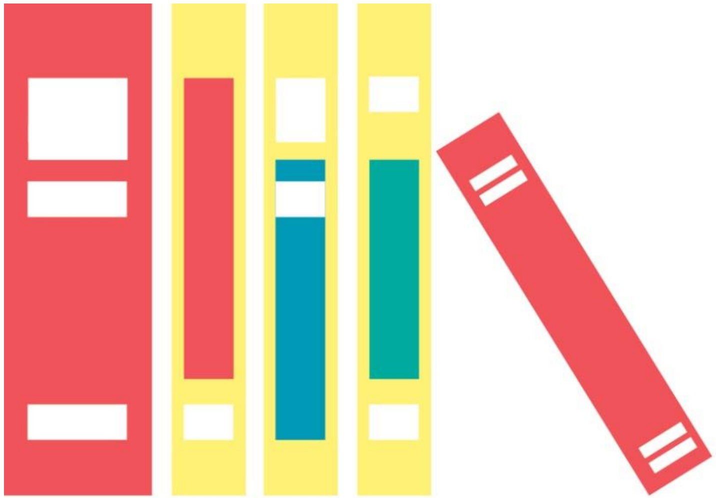
separate financials

- FV accounting for controlled investees in separate financials
- where exception applies to all subsidiaries in current and comparative periods: separates = consolidated

Accounting requirements - non-investment entity parent



Consolidation Package - Ind AS: 111 Joint Arrangements



Ind AS 111 definitions and terminology

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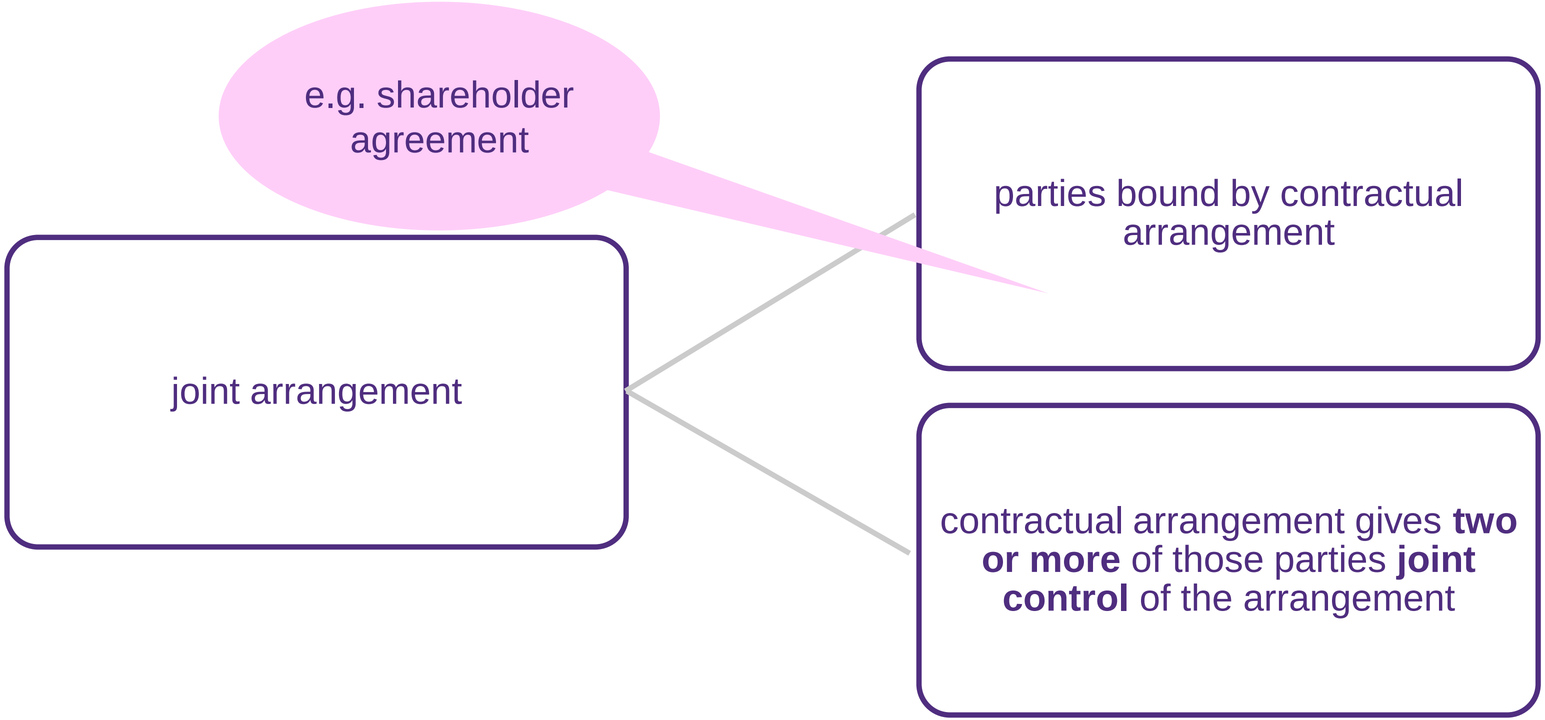
Joint arrangement	An arrangement of which **two or more parties** have **joint control**
Joint control	The **contractually** agreed sharing of control of an arrangement, which exists only when decisions about the **relevant activities** require the **unanimous consent** of the parties sharing control
A party to a joint arrangement	An entity that participates in a joint arrangement, regardless of whether that entity has joint control of the arrangement
Collective control	When **all the parties, or a group of the parties,** must act together to **direct** the activities that significantly affect the returns of the arrangement (i.e. the **relevant activities**)

Characteristics of a joint arrangement



Joint control?

Does a contractual arrangement give all the parties, or a group of parties, control of the arrangement collectively?

N → Outside the scope of Ind AS 111 (no joint control)

Y ↓

Collective control exists when all the parties, or a group of the parties, must act together to direct the relevant activities

Do decisions about the relevant activities require the unanimous consent of all the parties, or a group of parties, that collectively control the arrangement?

N → Outside the scope of Ind AS 111 (no joint control)

Y ↓

There is joint control (the arrangement is a joint arrangement)

Case studies 8, 9 and 10

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Case study 8: Implicit joint control

Case study 9: Minimum required proportion of voting rights

Case study 10: 'De facto' joint control

Definitions continued…

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Joint operation	A **joint arrangement** whereby the parties that have joint control of the arrangement have **rights to the assets, and obligations for the liabilities,** relating to the arrangement
Joint venture	A **joint arrangement** whereby the parties that have joint control of the arrangement have **rights to the net assets** of the arrangement
Joint operator	A **party to a joint operation** that **has joint control** of that joint operation
Joint venturer	A **party to a joint venture** that **has joint control** of that joint venture

Classification of a joint arrangement

Not structured through a separate vehicle

Structured through a separate vehicle

Evaluate rights and obligations of the parties:

- Legal form of the separate vehicle
- Terms of the contractual arrangement
- When relevant, other facts and circumstances

Rights to the assets, and obligations for the liabilities

Rights to the net assets

Joint operation

Joint venture

Takeaways

- Arrangements structured through a **separate vehicle** will normally (but not always) be a **joint venture** which must be **equity accounted**

- The **mechanics** of accounting for a **joint operation** may not always be the same as proportionate consolidation

Financial Statement (FS) of a joint operator

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FS of a joint operator

- Its revenue from the sale of its share of the output arising from the joint operation
- Its share of the revenue from the sale of the output by the joint operation
- Its expenses, including its share of any expenses incurred jointly
- Its assets, including its share of any assets held jointly
- Its liabilities, including its share of any liabilities incurred jointly

FS of a joint venturer

joint venturer (with joint control) → equity method → Ind AS 28

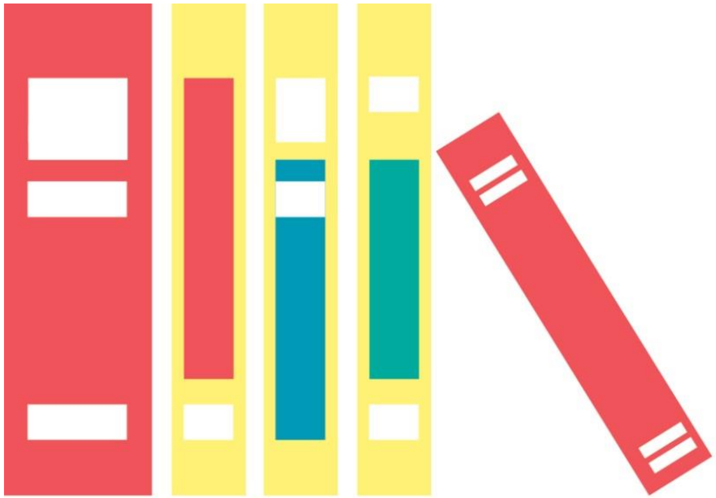
(Except if eligible for an exemption)

Other requirements - separate financial statements

separate financial statements of investors that share joint control

joint venturer	joint operator
either at cost or under Ind AS 39 (Ind AS 109) in accordance with Ind AS 27	applies same accounting as in consolidated f/s (accounts for its interest in the underlying assets and liabilities)

Consolidation - Ind AS 112: Disclosure of Interests in Other Entities



Scope

An entity is required to apply Ind AS 112, if it has an interest in one or more of the following:

- subsidiaries
- joint arrangements (joint operations or joint ventures)
- associates; and
- unconsolidated structured entities

Significant judgements and assumptions

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Significant judgements and assumptions (and changes) the entity has made in determining

- That it has control of another entity (Ind AS 110)
- That it has joint control of an arrangement or significant influence over another entity (Ind AS 111 and Ind AS 28)
- The type of joint arrangement
  - When structured through a separate vehicle

Significant judgements and assumptions

An entity should disclose significant judgements and assumptions made when determining that:

- it doesnot control another entity despite holding more than half of that other entity's voting rights;
- it controls another entity despite holding less than half of that other entity's voting rights;
- it is an agent or a principal
- it does not have significant influence over another entity despite holding 20% or more of that other entity's voting rights
- it has significant influence over another entity despite holding less than 20% of that other entity's voting rights

Interests in subsidiaries

This includes information about:

- Group composition
  - enable users to understand the composition of the group
- Interests of non-controlling interests (NCI) in group activities and cash flows, and
  - information about each subsidiary that has material NCI, such as
    - subsidiary's name,
    - subsidiary's principal place of business
    - summarised financial information (example included below)
    - dividend paid to NCI
    - accumulated NCI interest at the end of the reporting period
    - proportion of subsidiary's ownership interest held by NCI
- Significant restrictions on access to assets and obligations to settle liabilities
  - example of restrictions: statutory / regulatory / contractual restrictions

Interests in joint arrangements and associates

Detailed disclosures include:

- the name, country of incorporation and principal place of business;
- proportion of ownership interest and measurement method (equity or fair value method);
- If measured using equity method and there is a quoted market price for the investment, its fair value;
- summarised financial information;
- significant restrictions on the ability to transfer funds or repay loans;
- year-ends of joint arrangements or associates if different from the parent’s; and
  - date of the end of reporting period
  - reason for using a different date or different period
- unrecognised share of losses, commitments and contingent liabilities.
- risk associated with interest in joint ventures and associates
- contingent liability and commitment (reporting entity shall disclose seperately)

Interests in unconsolidated structured entities

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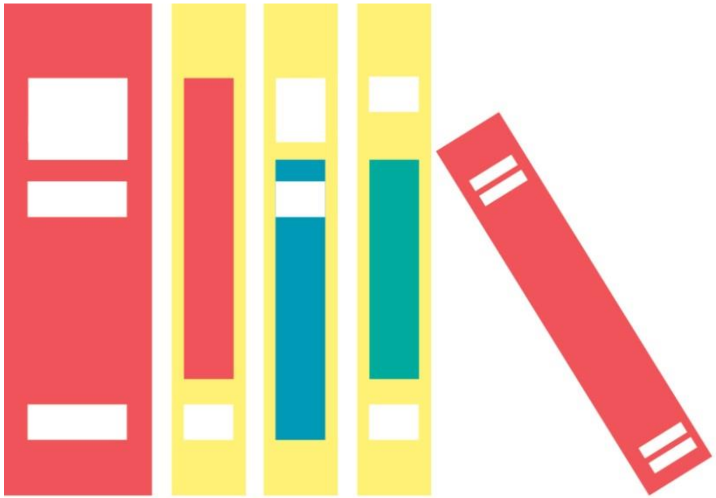
Detailed disclosures include:

- the nature, purpose, size, activities and financing of the structured entity;
- the policy for determining structured entities that are sponsored;
- a summary of income from structured entities;
- the carrying amount of assets transferred to structured entities;
- the recognised assets and liabilities relating to structured entities and line items in which they are recognised;
- the maximum loss arising from such involvement;
- information on financial or other support provided to such entities, or current intentions to provide such support.

Thank you!



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Ind AS 18 Revenue

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Contents

1. Overview
2. Definition
3. Timing:
   - sale of goods
   - rendering of services
   - other key considerations
4. Measurement
5. Special topics

Overview

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Ind AS 18 Status	• Ind AS 18 has been finalized by ICAI and sent to NACAS for consideration • Very much in line with IAS 18 • Notification expected by MCA soon
Objective	Determines: • the **timing** for the **recognition** of **revenue** • the **amount** of **revenue to be recognised**
Scope	Revenue from: • the **sale of goods** • the **rendering of services** and • the use by others of entity assets yielding **interest, royalties and dividends**
Core principle	Revenue is recognised when it is **probable** that **future economic benefits** will flow to the entity and these benefits can be **measured reliably**

Definition

Revenue is:

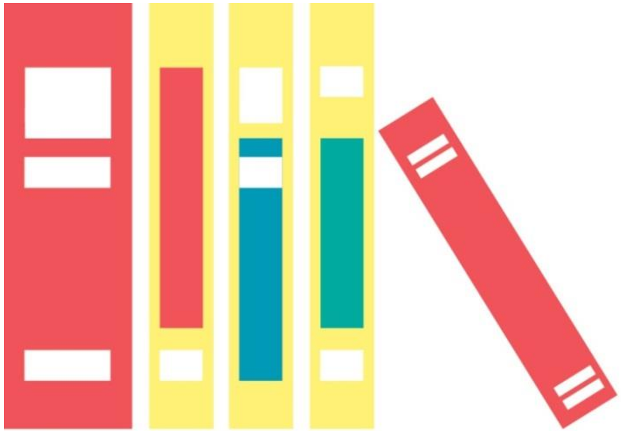
- the **gross** inflow of **economic benefits** during the period
- arising in the **course** of the **ordinary activities**
- result in **increases** in equity, other than increases relating to **contributions from equity participants**

Revenue excludes amounts collected

- on **behalf of third parties** (sales taxes, value added taxes and service tax)
  – for e.g. shipping and handling charges/ out of pocket expenses, if incurred on behalf of customer/ third party is not part of revenue. if the seller is not acting as an agent and generating additional margin, it is included in revenue
- by **an agent on behalf of the principal**

Excide duty for the purpose of presentation is not shown as part of revenue under Indian GAAP

Timing: Sale of goods



Timing

Sale of goods

Revenue from the **sale of goods** should be **recognised** when:

- **Transfer** of **significant risks and rewards of ownership of the goods**
- **No continuing managerial involvement** w.r.t **ownership** nor **effective control over the goods sold**
- revenue can be **measured reliably**
- **probable** that the **economic benefits** will flow
- **costs incurred or to be incurred** can be **measured reliably.**

Timing

Sale of goods: Transfer of significant risks and rewards

Usually happens when **legal title** or **possession of goods is transferred** to buyer**.**

Transfer of risks and rewards may occur before or after delivery

Situations where transfer of significant risks and rewards criterion is not satisfied:

- An entity retains obligation for unsatisfactory performance not covered under warranty
- When receipt of revenue is dependent upon buyer selling the goods and receiving the same.
- When goods are sold subject to installation and installation is significant part of sale
- When goods are sold on returnable basis and seller is not sure whether goods will be returned or not.

Example 1

Sale of goods: Transfer of risks and rewards

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- Entity A is a **manufacturer of engineering** and **heavy equipment**
- Entity A has manufactured an item of equipment according to the requirements of the customer (but not a **construction contract**)
- **legal title passes** when the **customer accepts delivery**
- the customer **accepts delivery** when **the assembly and installation** is complete in accordance with his requirements
- at 31 March 2014 the equipment has been physically delivered but the customer **was not satisfied** with the installation and required **major modifications**
- at 30 April 2014, after modifying the equipment to meet the customer's requirements, the customer **was satisfied** with the **modifications** and accepted the equipment
- Reporting date for the entity is **31 March** of every year.

When Entity A should recognise revenue i.e.in the year 2014 or 2015?

Solution

Sale of goods: Transfer of risks and rewards

Revenue from the **sale of goods** should be **recognised** when:

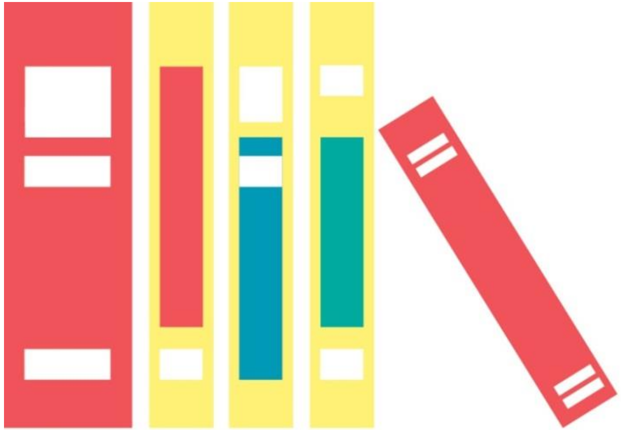
- the entity has **transferred** to the buyer the **significant risks and rewards of ownership of the goods**…

Therefore, Entity A **cannot recognise** the revenue on **31 March 2014** since the **risks and rewards of ownership** have not passed to the customer.
The equipment remains in inventory at 31 March 2014.

The fact that the client **has accepted the equipment at 30 April 2014** does not mean that Entity A can recognise the revenue on 31 March 2014.

It means that the **conditions for recognising revenue** have been met at **30 April 2014** and therefore the **revenue** should be recognised in the **year ending 31 March 2015**.

Timing: Rendering of services



Timing

Rendering of services

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In case of **rendering of services**, revenue should be recognized when the **outcome of a transaction** can be estimated **reliably,** in reference to the **stage of completion.**

The outcome of a transaction can be estimated **reliably** when:

- revenue can be **measured reliably**
- **probable** that the economic benefits will flow
- **stage of completion** can be measured **reliably**
- the **costs** incurred and the **costs to complete the transaction** can be measured **reliably.**

Timing

Rendering of services

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- **stage of completion** to be determined based on:
  - surveys of work performed
  - services performed as percentage of total services
  - cost incurred till date in proportion to total estimated costs

- in case of **indeterminate number of acts,** revenue should be recognized on **straight line basis** unless another method gives better reflection of stage of completion

- where **outcome of contract cannot be determined**, revenue needs to be recognized to the **extent of costs incurred**, provided costs are recoverable

- where a contract contains a **specific act**, which is **significant to the contract**, revenue is recognized when that **act is performed or completed.**

Example 2

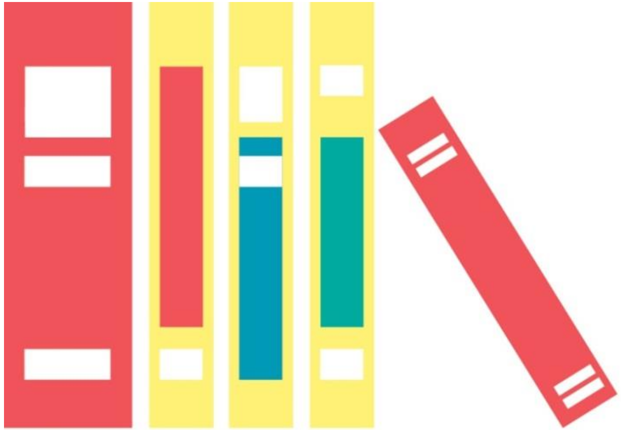
Timing: Rendering of services

- Entity A is a **financial services firm**
- in the **advisory service line**, Entity A receives **remuneration** on the basis of **time spent in advising to clients**. The remuneration is INR 1,000 per hour
- until 31 March 2015, Entity A has spent 100 hours on **advising a multinational automaker**

What is the amount of revenue that Entity A should recognise on 31 March 2015?

Entity A should recognise revenue based on the actual hours worked:
100 hours*INR 1,000= INR 1,00,000

Timing: Other key considerations



Timing

Other key considerations

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Nature	Criteria
Interest income	Using the effective interest rate
Dividend income	right to receive the dividend is established
Royalties income	On accrual basis in accordance with the terms of the agreement
Licensing income	Only on completion of performance under the contract
General Conditions for all	• amount of revenue can be measured reliably • the flow of economic benefits are probable

Example 3
Dividends

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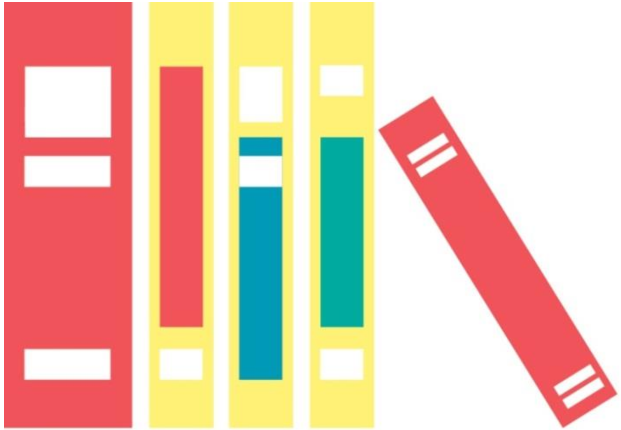
- on 1 July 2014 entity A has **acquired** 100 shares of entity B
- on 28 February 2015, Entity B **proposed** a dividend for the year ended 31 March 2015.
- The dividend payout is subject **approval** by the shareholders of entity B
- on **31 May 2015** the dividend was **approved** by the shareholders of Entity B at the annual general meeting. The dividend will be paid on 15 June 2015 to owners of Entity B's shares on 31 March 2014

When Entity A should recognise dividend income i.e.in the year 2014 or 2015?

- 31 March 2014: entity A should **not** recognise **dividend revenue**
- 31 March 2015: entity A **should recognise dividend revenue**

Measurement: Sale of goods and rendering of services



Measurement

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- revenue is measured at the **air value** of **consideration received/ receivable** after deducting **trade discounts** or **volume rebates** or **any other incentives**
- In case of significant gap between the date of sale and receipt of consideration, **time value of money** should be taken into account
  - **Interest income** is recognized as discount unwinds
- **fair value** is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date.

The **discount rate** is the more **clearly determinable of either:**

- the prevailing rate for a **similar instrument** of an issuer with a similar credit rating or
- a **rate of interest** that **discounts** the nominal amount of the **instrument** to the **current cash sales price.**

Example 4

Measurement: Rebates

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- Entity A is the **producer of luxury cars**
- Entity B is the **sole franchisee in India** for the selling of Entity A's luxury cars
- As per the contract if Entity B buys more than 1,000 units in 2015, it will receive a rebate of INR 5,00,000
- the price of each unit is INR 1,00,000
- on 30 September 2014, Entity B has purchased 520 units
- on 30 September 2014, the forecast purchases are 1,100 units in the year 2015
- Entity B bought 1,200 units during 2015.

What is the amount of revenue Entity A will recognise in the interim financial report for the first half of 2015 and the annual financial statements of 2015?

Solution

Measurement: Rebates

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As on 30 September 2014

As entity A has an obligation to pay rebate, it should adjust the revenue and recognise a provision for rebate as follows:

Rebate per unit
5,00,000/1,000 units = INR 500

Total amount	**5,20,00,000**	**520*1,00,000**
Rebate	2,60,000	520*500
Net Revenue	5,17,40,000	

As on 31 March 2015

Entity A must measure revenue from the sale of goods at fair value taking into account the amount of the rebate.

Therefore, it should measure revenue in the year 2015 at:

Total amount	**12,00,00,000**	**1200*100,000**
Rebate	5,00,000	520*500
Net Revenue	11,95,00,000	

Example 5

Measurement: Deferred payment

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- on 1 April 2014, Entity A has sold products to Entity B for INR **11,00,000** on **1 year interest free credit terms**
- recent cash price for similar purchases was **INR 10,00,000**
- what is the amount of revenue from sale of goods that Entity A will recognise in the year 2015?

How much revenue should be recognised by entity A?

Solution

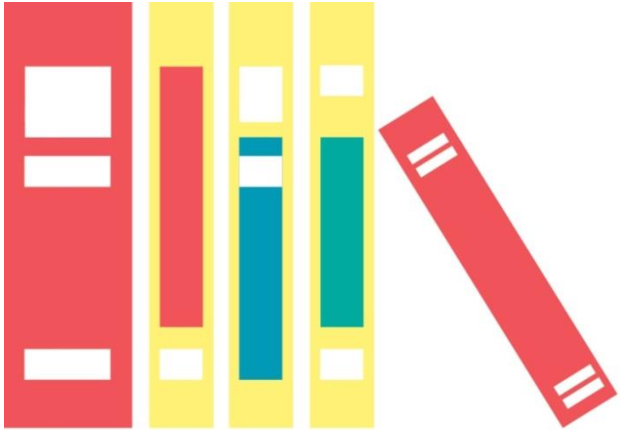
On 1 April 2014, Entity A should recognise **revenue from sale of goods** of **INR 10,00,000.**

Additionally, for year ended 31 March 2015, Entity A should recognise **interest income** of **INR 1,00,000** being **the finance element** of the transaction e.g. the **difference** between:

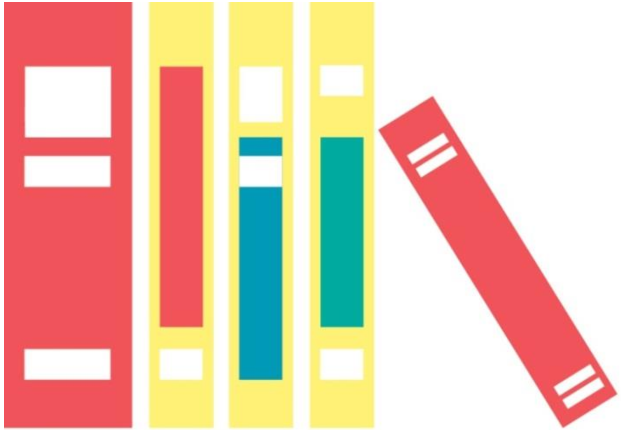
- the sale price of a transaction with **deferred payment**
- the **cash price**.

Special topics

- Multiple element arrangements
- Principal agent relationships
- Barter transactions
- Customer loyalty programmes
- Transfer of assets from customers



Multiple-element arrangements



Multiple-element arrangements

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The **recognition criteria** of **Ind AS 18** are **usually** applied **separately** to each **transaction**.

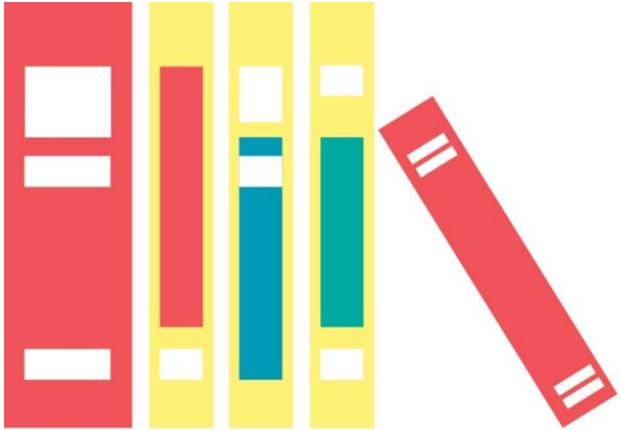
However, in certain circumstances, it is **necessary** to apply the recognition criteria to the **separately identifiable components** of **a single transaction** in order to reflect the **substance of the transaction**.

For example IT companies in case of transaction for sale of software also includes software license, implementation, development and AMC services.

In those cases revenue is recognized separately for:

- Revenue for sale of software: Based on sale of goods criteria
- Other components which include services: Based on sale of services criteria

Principal agent relationships



Principal agent relationships

Gross or net

- In an agency relationship, "gross" amounts collected by the agent **on behalf of the principal** are not benefits that flow to the agent and, therefore, are **not revenue**.
- The agent's revenue is the "net" amount of the commission.

Indicators of Agent

- The supplier (and not the seller) is the primary obligor in the arrangement.
- The seller earns a fixed or determinable amount.
- The supplier (and not the seller) has credit risk.

Principal agent relationship

Gross or net

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Indicators of principal:

- Is the primary obligor in the arrangement.
- Has general inventory risk (before the customer order is placed or on customer return).
- Has latitude in establishing price.
- Changes the product or performs part of the service.
- Has discretion in supplier selection.
- Is involved in determining product or service specifications.
- Has physical loss inventory risk (after the customer order or during shipping).
- Has credit risk.
- Is responsible for warranty or quality risk on the product(s) sold or service(s) rendered.

Example 6

Principal agent relationship: Gross or net

Entity A is manufacturer and distributor of food products. Entity B is a retailer who has agreed to sell the products of entity A on following terms:

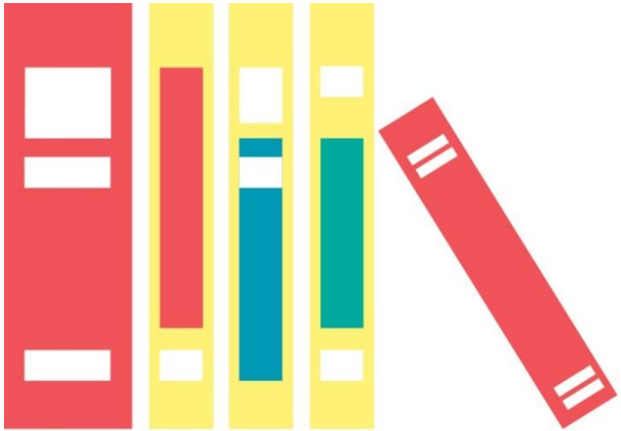
- B will store and sell the goods to customers
- B will earn a fixed margin on goods sold
- In case the goods are not sold, the same can be retuned to A
- B is responsible for goods only when they are in his store.
- A bear the credit risk

When B is acting as a principal or and agent in this relationship?

Solution:

B is acting as an agent.

Barter transactions



Barter transactions

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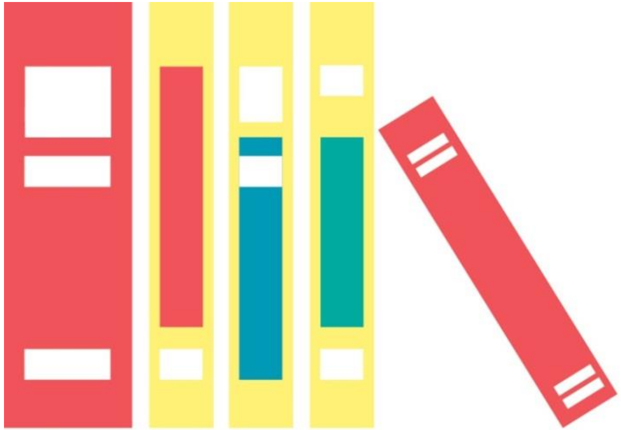
- revenue from a 'barter' transaction involving advertising **cannot** be measured **reliably** at fair value of advertising services

- seller **can reliably** measure **revenue** at **fair value** of **advertising services** provided in a **barter transaction** only by reference to **non-barter transactio** that:
  - involve advertising **similar** to the advertising in the barter transaction
  - occur **frequently**
  - represent a predominant number of transactions and amount when compared to all transactions to provide advertising that is similar to the advertising in the barter transaction
  - involve cash and/or another form of consideration that has a **reliably measurable fair value**
  - do not involve the same counterparty as in the barter transaction.

Customer loyalty programmes



Customer loyalty programmes

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- account for **award credits** as a **separate component** of revenue
- the **fair value** of the **consideration received or receivables** should be **allocated** between:
  - the **award credit** and
  - **other components of the transaction**

- recognise **revenue** when:
  - **award credits are redeemed** and
  - the entity **fulfils its obligations to supply awards**

- the amount of **revenue recognised** should be based on:
  - the number of **award credits** that have been **redeemed** in **exchange for awards** **RELATIVE**
  - to the **total number expected to be redeemed**.

Example 7

Customer loyalty programmes

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- retailer grants programme members loyalty points when they spend a specified amount in store. Programme members can redeem the points for further goods
- in the year 2014, retailer grants **10,000 points**. **Points do not expire**
- management **expects 9,000** of these **points to be redeemed**
- management **estimates the fair value** of each **loyalty point awarded to be INR 1**
- set out below the redemption of the points in exchange for goods at the end of the forthcoming years:

Date	Points redeemed
31/03/2015	4,500
31/03/20X6	4,100
31/03/20X7	400

What is amount of revenue that should be recognised?

Solution

Customer loyalty programmes

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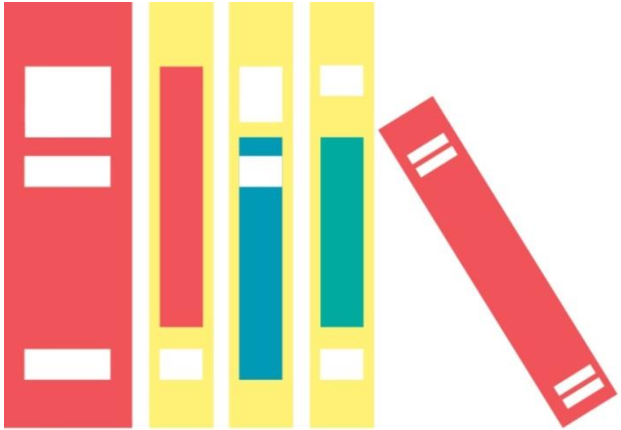
31 March 2014

Retailer initially defers **revenue** of **INR 10,000 (10,000 points * INR 1)**

31 March 2015- 31 March 20X7

Date	Points redeemed	Accumulative points redeemed	Accumulative Revenue	Annual revenue
31/03/2015	4,500	4,500	4,500/9,000 * INR 10,000= INR 5,000	INR 5,000
31/03/20X6	4,100	8,600	8,600/9,000 * INR 10,000= INR 9,556	INR 4,556 (9556-5000)
31/03/20X7	900	9,000	9,000/9,000 * INR 10,000= INR 10,000	INR 444 (10000-9556)

Transfer of assets from customers



Transfers of assets from customers

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31 March 2014

Retailer initially defers **revenue** of **INR 10,000 (10,000 points * INR 1)**

31 March 2015- 31 March 20X7

Date	Points redeemed	Accumulative points redeemed	Accumulative Revenue	Annual revenue
31/03/2015	4,500	4,500	4,500/9,000 * INR 10,000= INR 5,000	INR 5,000
31/03/20X6	4,100	8,600	8,600/9,000 * INR 10,000= INR 9,556	INR 4,556 (9556-5000)
31/03/20X7	900	9,000	9,000/9,000 * INR 10,000= INR 10,000	INR 444 (10000-9556)

Transfers of assets from customers

Asset and revenue recognition:

Does item received meet the definition of an asset (per the Framework)?

Yes

Recognise the asset
- measure at fair value
- Depreciate it over its useful life
- Allocate revenue based on service

Recognise revenue - pattern depends on the service to be provided to the customer

Type of services provided:
- connection service - recognise when service is provided
- ongoing access to supply of goods and services - over term of contract
- both services - allocate revenue between two components

No

No asset to be recognised

Example 8

Transfers of assets from customers

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A company provides outsourcing services of information technology (IT) functions to its customers.

- Customer transfers ownership of its IT asset to the company for providing services.
- Company is responsible for maintaining the equipment.
- Useful life of the equipment is 3 years.
- Agreement period is 10 years for a fixed price which is lower than price charged if the IT asset was not transferred.

How revenue should be recognized by the company?

Solution:

- The entity should recognize the equipment and measure its cost on initial recognition at its fair value.
- The company should recognize revenue from the exchange transaction over the 10 year period.

Alternatively

- If after the three years, the company replace the equipment and the price increases.
- Then the company should recognise revenue from the exchange transaction over the first three years of the agreement.

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Ind AS 11 Construction Contracts

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Contents

Overview

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Ind AS 11 Status	• Ind AS 18 has been finalized by ICAI and sent to NACAS for consideration • Ind AS 18 includes accounting in respect of real estate developers, which is not in scope of IAS 11 • Notification expected by MCA soon
Objective	Prescribes the **accounting treatment** of **revenue** and **costs** associated with **construction contracts**
Scope	The **accounting treatment** for **construction contracts** in the financial statements of **contractors** including **real estate developers**
Core principle	• revenue is recognised at **fair value** of the **consideration received** • recognise **revenue** and **costs** by reference to the **stage of completion** when the outcome of a construction contract **can** be estimated **reliably** • if the outcome of a construction contract **cannot** be estimated **reliably** then revenue should be recognised only to the extent of contract costs incurred that it is probable will be **recoverable**

Definition

"A contract **specifically negotiated** for the **construction** of an **asset** or a **combination of assets** that are closely **interrelated or interdependent."**
Also includes agreements of **real estate development** providing **services** with **construction material**

Examples for **single assets within** the **scope** of **Ind AS 11**:

- bridge
- building
- dam
- pipeline
- road
- ship
- tunnel.

Examples for closely **interrelated or interdependent assets within the scope of Ind AS 11**:

- refineries
- complex pieces of plant or equipment.

Combining & segmenting of construction contracts

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Combine

- negotiated as a **single package**
- so **closely interrelated** that they are, in effect, a **single project**
- contracts **performed concurrently** or in a **continuous sequence**.

Segment

- separate **proposals submitted** for each asset
- each asset subject to a **separate negotiation**
- **cost and revenues** for each asset can be **identified.**

Contract revenue

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- **revenue** is recognised at **fair value** of the **consideration received** and comprises:
  - the **initial amount** of **revenue agreed** in the **contract** and
  - **variations** in **contract work, claims** and **incentive** payments:
    - to the extent that it is **probable** that they will result in **revenue** and
    - if they are capable of being **reliably measured.**

Contract costs

- costs that relate **directly** to the **specific contract**:
  - site labour, including **site supervision**
  - **materials** used in **construction**
  - **depreciation** of plant and equipment used
  - moving plant, equipment and materials **to / from** the **contract site**
  - **estimated costs** of **rectification** and **guarantee work**
- costs that are **attributable** to **contract activity** in general and can be **allocated** to the **contract**:
  - **insurance**
  - design and technical assistance not directly **related to a specific contract**
  - **construction overheads**
  - borrowing costs
- such other costs as are **specifically chargeable** to the customer under the terms of the contract.

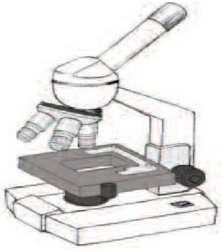
Recognition of contract revenue and expenses

In case, when the outcome of a construction contract **can** be estimated **reliably:**
Recognise contract revenue and contract costs by reference to the **stage of completion** of the **contract activity** (**percentage of completion method**)

When the outcome of a construction contract cannot be estimated reliably:

- revenue should be recognised only to the extent of contract costs incurred that it is probable will be recoverable and
- contract costs should be recognised as an expense in the period in which they are incurred.

When it is **probable** that **total contract costs** will **exceed total contract revenue**, the **expected loss** should be recognised as **an expense immediately.**



Example 9

Reliable outcome

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Set out below details about **construction contract 1** in the year 2015:

Contract 1

Estimated total revenue		100
Costs to date		48
Costs to complete	32	
Total estimated costs		80
Stage of completion		**60%**

What is the **accounting treatment** for the year ended 31 December 2015 in accordance with **Ind AS 11**?

Solution

Reliable outcome

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Contract 1

Estimated total revenue		100
Costs to date		48
Costs to complete	32	
Total estimated costs		80

Stage of completion 60%

60%

P&L for the year 2005

Revenue	60	
Cost of sales		(48)
Profit		12

Example 10
No reliable outcome

Set out below details about **construction contract 2** in the year 2015:

Contract 2

Estimated total revenue		100
Costs to date		10
Costs to complete	?	
Total estimated costs		?

Assume that the **outcome** of the **contract cannot** be **estimated reliably and the Entity expects** that the costs incurred will be **recovered.**

What is the **accounting treatment** for the year ended 31 December 2015 in accordance with **Ind AS 11**?

Solution

No reliable outcome

Contract 2

Estimated total revenue	100
Costs to date	10
Costs to complete	?
Total estimated costs	?

P&L for the year 2005

Revenue	10
Cost of sales	(10)
Profit	-

Example 11
Loss outcome

Set out below details about **construction contract 3** in 2015:

Contract 3

Estimated total revenue		100
Costs to date		72
Costs to complete	48	
Total estimated costs	120	
Stage of completion		**60%**

What is the **accounting treatment** for the year ended 31 December 2015 in accordance with **Ind AS 11**?

Solution

Loss outcome

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Contract 3

Estimated total revenue	100
Costs to date	72
Costs to complete	48
Total estimated costs	120

Stage of completion 60%

60%

P&L

Revenue	60
Cost of sales	(72)
Balancing figure	(8)
Loss	(20)

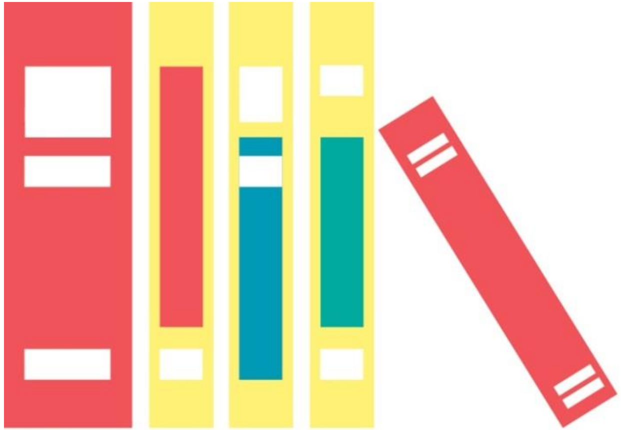
Disclosures

- contract **revenue recognised in the period**
- details of **methods used to determine contract revenue** recognised in the period
- details **of methods used to determine stage of completion of contracts in progress**
- contract costs incurred & recognised profits to date
- gross amount due from **customers for contract work as an asset**
- gross amount due to **customers for contract work as a liability**
- the amount of **advances received**.

Status of the ICAI 's new revenue standard

- ICAI has issued exposure draft, of Ind AS 115 *Revenue from Contracts with Customers* corresponding to IFRS 15
- Final Standard is expected in few months.
- This Module provides understanding of existing Standards and Interpretations on revenue and construction contracts.
- The new Revenue Standard will supersede:
  - Ind AS 18: Revenue
  - Ind AS 11: Construction Contracts
  - Ind AS 11: Appendices: Service Concession arrangement and disclosures

Thank you!



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Ind AS 11 - Appendix A & B
Service Concession Arrangements & Disclosures

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Service Concession Arrangements

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Service arrangements is the public service nature of the obligation undertaken by the operator. The arrangement obliges the operator to provide services to the public on behalf of the public sector entity.

Other common features are:

- party that grants the service arrangement (the grantor) is a public sector entity.
- the operator is responsible for at least some of the management of the infrastructure and related services
- the contract sets the initial prices to be levied by the operator and regulates price revisions
- the operator is obliged to hand over the infrastructure to the grantor in a specified condition at the end of the arrangement, for little or no incremental consideration

Service Concession Arrangement – Example

- Toll roads
- Metro Railway Station
- Airports
- Hospitals
- City swimming pools
- Golf courses

Applicability

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The appendix is applicable to both:

- **infrastructure** was either **constructed or acquired by operator** from a third party for the purpose of the concession.

  &

- **Existing infrastructure given by grantor** to the operator for concession.

Applies to public-to-private service concession arrangements if:

- **grantor regulates** services provided, to whom it is provided to and at what **price**

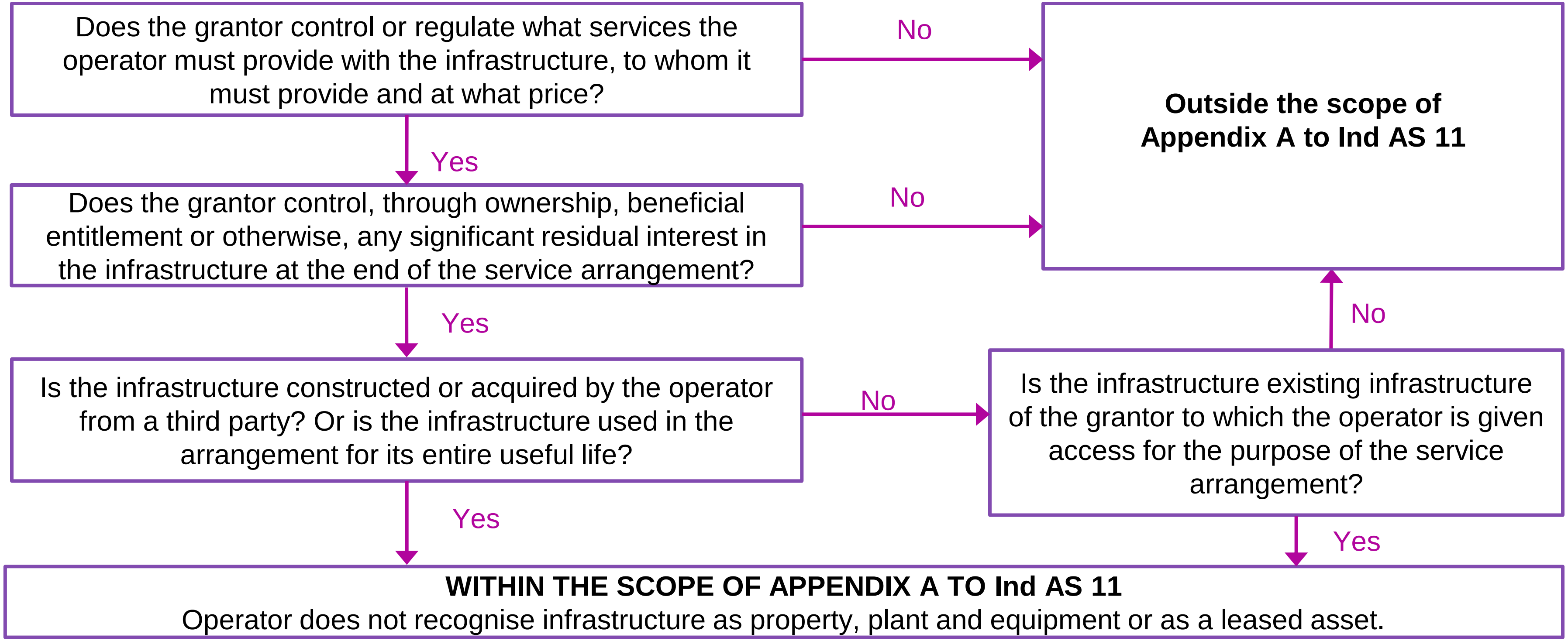
  &

- **grantor controls** any **significant residual interest** in the **infrastructure** at end of arrangement

Appendix A to Ind AS 11 deals with the accounting treatment by operators

Applicability deferred under Ind AS

Applicability



Public to Private Arrangements

<table>
<tr><th>Category</th><th>Lessee</th><th colspan="3">Service Provider</th><th colspan="2">Owner</th></tr>
<tr><td>Typical Arrangement Types</td><td>Lease (eg. operator leases asset from grantor)</td><td>Service and/or maintenance contract (specific tasks eg. collection of debt)</td><td>Rehabilitate Operate Transfer</td><td>Build Operate Transfer</td><td>Build Own Operate</td><td>100% Divestment/ Privatisation Corporation</td></tr>
<tr><td>Asset Ownership</td><td colspan="4">Grantor</td><td colspan="2">Operator</td></tr>
<tr><td>Capital Investment</td><td colspan="2">Grantor</td><td colspan="4">Operator</td></tr>
<tr><td>Demand Risk</td><td>Shared</td><td>Grantor</td><td colspan="2">Operator and/or Grantor</td><td colspan="2">Operator</td></tr>
<tr><td>Typical Duration</td><td>8-20 years</td><td>1-5 years</td><td colspan="3">25-30 years</td><td>Indefinite (or may be limited by license)</td></tr>
<tr><td>Residual Interest</td><td colspan="4">Grantor</td><td colspan="2">Operator</td></tr>
<tr><td>Relevant Ind AS</td><td>Ind AS 17</td><td>Ind AS 18</td><td colspan="2">Ind AS 11 Appendix A</td><td colspan="2">Ind AS 16</td></tr>
</table>

Initial Recognition

The **operator** does not recognise concession infrastructure as its **PP&E.**

The **operator accounts for revenue** and **costs** in accordance with **Ind AS 11** and **Ind AS 18**

- If the operator performs both, construction/ upgrade and operation services in a single contract, consideration is allocated to their relative fair values, if amounts are separately identifiable.

The **operator** should record a **financial asset** or an **intangible asset** depending on the **character** of the **receivable**

- **financial asset** if there is unconditional right to receive cash or other financial asset from the grantor
- **intangible asset** if it receives a right (e.g., licence) to charge users

Service Concession - Examples

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Quick Quiz	Recognise as Financial or Intangible asset
Operator receives a fixed or determinable payments from the grantor without any risk.	Financial Asset
Grantor pays operator based on usage	Intangible Asset
User pays operator based on usage	Intangible Asset
Users pay operator but price is regulated by grantor to ensure that operator receives a fixed return on its investment.	Intangible Asset
Users pay operator for use of infrastructure and grantor pays shortfall, if any between actual revenue and guaranteed revenue	Financial Asset Or both

Measurement

Particulars	Ind AS	Financial asset	Intangible asset
Construction revenue and cost incurred during the construction period	Ind AS 11	Percentage Completion Method	
Revenue and costs relating to operation services incurred by the operator	Ind AS 18		
Contractual obligations to maintain or restore infrastructure	Ind AS 37	PV of the expenditure required to settle the obligation	
Borrowing cost incurred during the construction phase	Ind AS 23	Charged to P & L	Capitalise

Measurement – Intangible Assets Model

Right to charge users for the service is **measured at cost** i.e. the fair value of consideration transferred to acquire the asset.

As per Ind AS 38, the intangible asset is **amortised** over the period, it is **available for use** by the operator i.e. on **straight line basis.**

Schedule II of the Companies Act, 2013, allows revenue based amortisation in case of Intangible Assets: Toll Road

Case Study – Intangible Asset Model

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The operator constructs a bridge at a cost of INR 500. Profit under the arrangement is estimated at INR 50 and the contractual cash flows from the user are expected to be INR 1000 over the period of the contract.

Initial Recognition

Intangible asset will be recognised at fair value of the cost incurred plus the profit margin i.e. INR 550

Subsequent Measurement

Amortise intangible asset over life of intangible i.e. INR 550 over the period of the agreement

Accounting of Revenue and costs

- During the period of construction – Ind AS 11
- After the period of construction - Ind AS 18

Measurement – Financial Asset Model

The amount due is accounted in accordance with Ind AS 39 as:

- a loan or receivable
- an available-for-sale financial asset (AFS)
- fair value through profit or loss, if conditions are met.

If classified as loan or receivable or as AFS, interest to be calculated using the effective interest method to be recognised in profit or loss

Case Study – Financial Asset Model

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The operator constructs a bridge at a cost of INR 500. Profit under the arrangement is estimated at INR 50 and the contractual cash flows from the grantor are expected to be INR 1000 over the period of the contract.

Initial Recognition

Intangible asset will be recognised at fair value i.e. INR 550

Subsequent Measurement

Amortise financial asset of INR 550 as the operator receives cash, over the period of agreement

Recognise finance income of INR 450 over the period of the agreement

Disclosures

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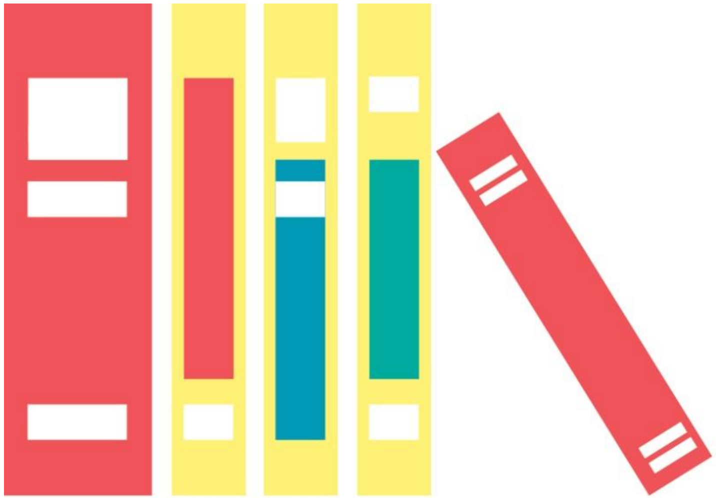
An **operator** and a **grantor** shall disclose the following in each period**:**

- a description of the arrangement
- **significant terms** of the arrangement that may affect the amount, timing and certainty of future cash flows
- the **nature and extent** (e.g. quantity, time period or amount as appropriate) of:
  - rights to use **specified assets**
  - obligations to provide or rights to expect provision of services
  - obligations to acquire or build items of **PP&E**
  - obligations to deliver or rights to receive **specified assets** at the end of the concession period
  - renewal and **termination options**
  - other rights and obligations (e.g. major overhauls)
- changes in the arrangement occurring during the period
- how the service arrangement has been **classified**.

Operator to disclose the amount of revenue and profits/ losses recognised in the period.

Disclosures shall be given separately for each arrangement or in aggregate for each class of arrangements.

Thank you!



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Ind AS 20 Government Grant

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Overview

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Objective	Sets out the accounting and disclosure of **government grants** and similar assistance
Scope	Accounting and disclosure of government grants and government assistance **except**: • **government grants** in **hyperinflationary economies** • **government grants** in the **form of tax benefits** • **government participation** in the ownership of an entity • **government grants** within the scope of **Ind AS 41**
Core principle	**Government grants**, including **non monetary grants**, is recognised when there is **reasonable assurance** that: • the entity will **comply** with the **necessary conditions** and • the **grant** will be **received**
Key definitions	• **government assistance** • **government grants**

Definition

- **Government grant**
  - assistance by government in the form of transfers of resources
  - in return for past or future compliance with certain conditions
  - relating to the operating activities

- **Government assistance**
  - action by government
  - to provide an economic benefit
  - specific to an entity or range of entities qualifying under certain criteria

- Government Grant excludes assistance with no value and transactions with government which are normal trading transactions

- Government grant is also know as subsidies, subventions, or premiums.

Example – Government Grant and Assistance

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Government grant	Government assistance
Providing freehold land	Free technical advice / marketing advice
Provision of money for purchase of machinery	Provision of guarantees
Government aid towards setting up a new plant in remote area	Government procurement policy – responsible for company's portion of sales

Recognition

Recognition of government grant

- **Compliance with conditions attached**
- **Reasonable assurance**
- **Receipt of grant**

- **Under Ind AS 20, non-monetary government grants, e.g., land given free of cost, are measured at fair value**
- **Ind AS 20 gives an option to measure non-monetary government grants either at their fair value or at nominal value**

Recognition - approach

Government grant

- **Capital approach**
  - Recognition outside P&L
- **Income approach**
  - Recognition in P&L
    - On systematic basis over the period
      - Related directly to incurring specific expenditures
        - same period as the relevant expenses
      - Related to acquisition of assets - Depreciable
        - In the proportions in which depreciation

Presentation

- **Presentation**
  - **Asset Grant**
    - Deferred income
    - Deducted from carrying amount
  - **Income Grant**
    - Credited in P&L separately or disclosed under other income
    - Deducted from related expense

As per Ind AS 20 asset related grants shall be presented as deferred income in the balance sheet

Presentation

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- **Presentation**
  - **Asset Grant**
    - Deferred income
    - Deducted from carrying amount
  - **Income Grant**
    - Credited in P&L separately or disclosed under other income
    - Deducted from related expense

As per Ind AS 20 asset related grants shall be presented as deferred income in the balance sheet

Presentation – Example (Asset Grant)

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- XYZ Ltd. receives a INR 5,000 grant toward the purchase of new equipment
- Cost of equipment - INR 20,000;
- Life of equipment - 5 years
- Method of depreciated - straight-line

Presentation – Solution (Asset Grant)

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Deferred Income

Year 1

Bank a/c	Dr. 5,000
To Deferred Government grant a/c	Cr. 5,000

Subsequently (When asset is used)

Depreciation a/c	Dr. 4,000
To Accumulated depreciation a/c	Cr. 4,000
Deferred government grant a/c	Dr. 1,000
To Grant income a/c	Cr. 1,000

Deduction from carrying amount

Year 1

Bank a/c	Dr. 5,000
To Equipment a/c	Cr. 5,000

Subsequently (When asset is used)

Depreciation a/c	Dr. 3,000
To Accumulated depreciation a/c	Cr. 3,000

Presentation – Income Grant

XYZ Ltd. receives 20% of its labor cost as government grant.
Total labor cost is INR 10,000

Option 1:

Bank	a/c	Dr. 2,000
To Grant income		Cr. 2,000

Option 2:

Bank	a/c	Dr. 2,000
To Labor cost		Cr. 2,000

Repayment

Repayment of government grant – to be treated as "Change in estimate"

Repayment of government grant

- **Related to an asset**
  - **Cumulative amount of additional depreciation**
    - **Recognised to current year profit or loss**
- **Related to income**
  - **Any necessary adjustments**
    - **Adjusted to current year profit or loss**

As per Ind AS 20 repayment of a grant related to an asset shall be recognised by reducing the deferred income balance by the amount repayable.

Disclosures

- the **accounting policy** adopted for **government grants**, including the **methods of presentation**
- the **nature and extent** of **government grants** recognised and an **indication** of other forms of **government assistance**
- **unfulfilled conditions** and other **contingencies attaching to government assistance** that has been recognised.

Thank you!