Ind AS Annual report card

September 2017

Contents

Section	Page
Foreword	4
Background of Ind AS	6
Impact summary	7
Sector-key accounting area analysis matrix	7
Accounting analysis: Common areas of impact	11
Accounting analysis: Industry Wise impact	20
Automotive and ancillary	21
Construction, engineering and infrastructure	25
Manufacturing	29
Power	33
Real estate	36
Telecommunication	39
Chemicals and fertilizers	42
Information technology	45
Media and Entertainment	49
Oil, gas and mining	53
Retail	56
Pharma Industry	57
Logistics	60
Service	63
MAT implication for Ind AS adjustments	64
Key take-aways for CFOs	66
Glossary	67

Foreword

Ashish Gupta

Siddharth Talwar

The objective of this publication is to provide a qualitative analysis of the first financial results as per Ind AS reported by more than 500 listed companies for the year ended 31 March 2016.

India has finally joined the elite club of nations that have adopted the internationally recognised accounting norms. The steps to this milestone can be traced to almost a decade of efforts by several authorities and professionals and several practical challenges that came in at various stages.

The Leaders' Statement at G-20 Summit held in September 2009 at Pittsburgh contained a commitment by the G-20 nations for convergence to accounting standards ('AS') globally. The Statement read, "We call on our international accounting bodies to redouble their efforts to achieve a single set of high quality, global accounting standards within the context of their independent standard setting process, and complete their convergence project by June 2011. The International Accounting Standards Board's ('IASB') institutional framework should further enhance the involvement of various stakeholders."

In 2011, to keep up its commitment at the G-20 forum, the Institute of Chartered Accountants of India (ICAI) issued the IFRS converged standards, referred to as Indian Accounting Standards or "Ind AS". In March 2014, the ICAI issued a roadmap recommending adoption of Ind AS for preparing consolidated financial statements (to address taxation related matters) for accounting year beginning on or after 1 April 2016, along with comparatives for the previous financial year. In February 2015, Ministry of Corporate Affairs ('MCA') notified the final roadmap on Ind AS with implementation in phased manner to be complied by the specified class of companies with an effective date of 1 April 2016.

Post MCA's announcement, most Indian corporates visualised a long path for adapting to this new accounting change. Ind AS being converged to globally recognised International Financial Reporting Standards ('IFRS'), the key highlights of impact that Ind AS may have on financial reporting was known to most companies. However, the magnitude of impact was uncovered gradually as companies implemented Ind AS and reported their Ind AS results first time for quarter ended 30 June 2016. Some of the key challenges faced by companies during transition included:

(i) IT systems required re-configuration to facilitate dual reporting.

(ii) Tax considerations on the accounting impact of certain typical transactions under Ind AS are still shaping up.

(iii) Lack of trained accounting personnel.

(iv) Last-minute pressure with most companies that started late in the day.

While the non-financial services companies were gearing up to execute Ind AS in line with their road map announced by MCA, the excluded entities - banks, insurance companies & NBFCs - were soon covered as MCA laid down the roadmap for their Ind AS implementation. Keeping pace with the revolutionary changes in the accounting framework, standards with respect to the computation of tax viz. ICDS have been notified separately.

A reliable, consistent and uniform financial reporting framework is an important part of good corporate governance. Globalisation has broken all boundaries for investments and investors, therefore, there is a need for uniform globally accepted set of ASs to facilitate comparison. Grant Thornton India LLP supports the initiatives taken by several regulatory agencies in this convergence process. While we understand the unique landscape of Indian economy which necessitates divergence from IFRSs, on a larger note, we favour all steps taken to keep those differences to the minimum.

The objective of this publication is to provide a qualitative analysis of the first financial results as per Ind AS reported by more than 500 listed companies for the year ended 31 March 2016. This publication is not intended to be a technical guide for a deep dive into the complex world of accounting jargons. It is expected that this publication will provide an insight into why the numbers look different from what they were reported earlier and enable you to familiarise yourself with some of the key aspects of this historic transition that you, as business leaders, investors or informed users of financial statements must be aware of.

Given the ubiquity of this accounting change and its wide ranging impact, the necessary steps in the direction of implementing this fundamental change need to be taken now. As a piece of boardroom advice – we suggest that the management of companies should present their Board of Directors with an analysis of impact of Ind AS implementation and an action plan to implement the change. Making necessary tweaks to IT systems, ramping up the financial reporting teams, acquiring necessary international Generally Accepted Accounting Principles ('GAAP') accounting skills, identifying obstacles in fair valuation exercises and most importantly, making appropriate accounting policy choices, and other steps that need careful consideration.

We hope that this publication will provide financial reporting executives with an analysis of relevant industry practices for the Ind AS implementation process.

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Background of Ind AS

Before discussing the background of Ind AS, the roadmap for companies, banks, insurance companies and NBFCs is as follows:

Corporates		Non-banking financial companies (including Housing Finance Companies)		Banking companies/ Insurance companies
Criteria	**Period of reporting**	**Criteria**	**Period of reporting**	**Period of reporting**
Listed / Unlisted: Net worth => 500 Cr	2016-17	Listed / Unlisted: Net worth => 500 Cr	2018-19	Banking companies: 2018-19 or later (no net worth criteria)
Listed: Net worth <500 Cr Unlisted: 250 Cr <= Net worth < 500 Cr	2017-18	Listed: Net worth <500 Cr Unlisted: 250 Cr <= Net worth < 500 Cr	2019-20	Insurance companies: 2020-21 or later (no net worth criteria)

In line with IFRS requirements, companies shall be required to prepare their first set of financial statements in accordance with Ind AS effective at the end of their first Ind AS reporting period. Application of Ind AS is irrevocable, even if an entity, which has adopted Ind AS, does not fall under the threshold for applicability of Ind AS in any subsequent year.

There were two major changes globally in the accounting standards brought by the IASB – "revenue recognition" (IFRS 15) and "financial instruments" (IFRS 9). It is important to understand that globally, 130 plus countries follow IFRS as issued by the IASB and would apply IFRS 9 from annual period beginning on or after 1 January 2018. It may be noted that in India, MCA has notified standard on financial instruments, Ind AS 109 based on the global standard IFRS 9, which is applicable for the companies covered in phase 1 as per the corporate road map from 1 April 2015. However, for "revenue recognition" standard, Indian corporates are currently aligned with globally applicable requirements.

Ind AS has a specific standard on transition to the new financial reporting framework (Ind AS 101). It provides certain optional exemptions and mandatory exceptions to entities for ensuring a smooth transition from existing accounting practices. It is important that accounting professionals and CFOs make informed accounting policy choices that will be available upon transition.

The dynamic business landscape and growing business complexities pose significant challenges in transitioning to the new financial reporting framework for Indian corporates. The drivers of these challenges are diverse, inter-alia:

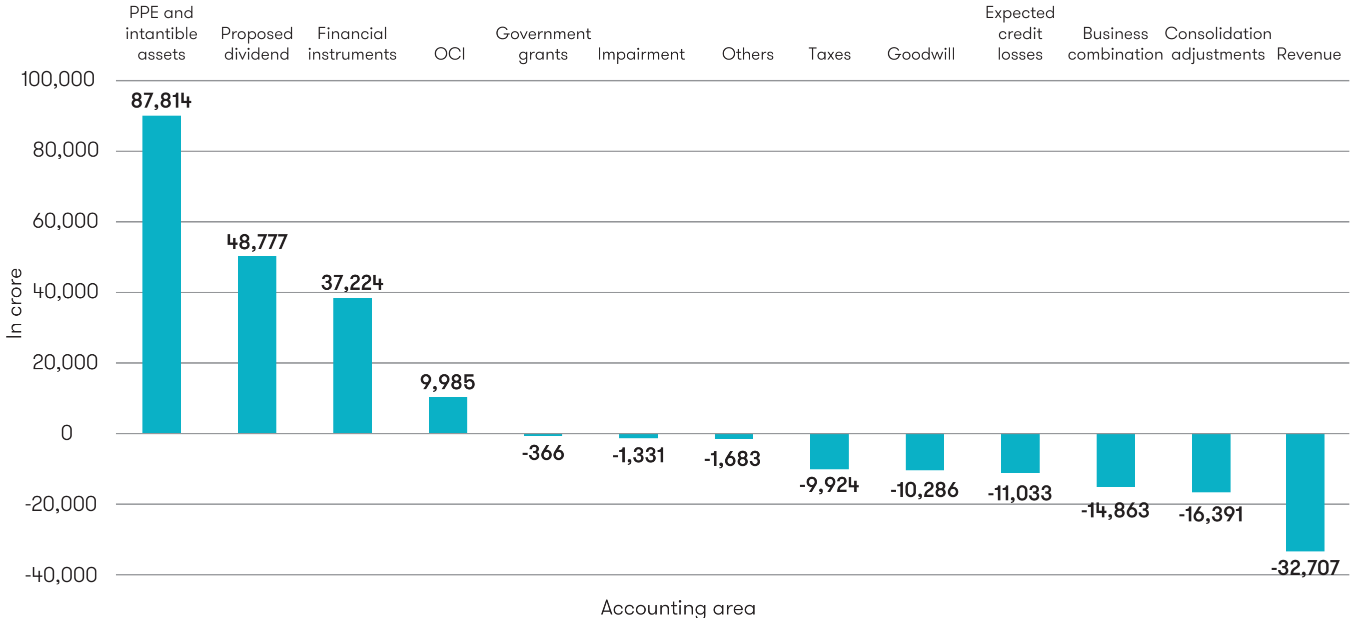
- accounting policy choices available under the transition standard
- increasing size and complexity of business transactions
- increasing pressure to publish financial information faster
- continuously evolving accounting standards, guidance and references
- multiplicity of accounting practices and standards across subsidiaries and segments
- quality of accountants available for data processing and validation

Accordingly, it is imperative for a company to define a process whereby the following is achieved:

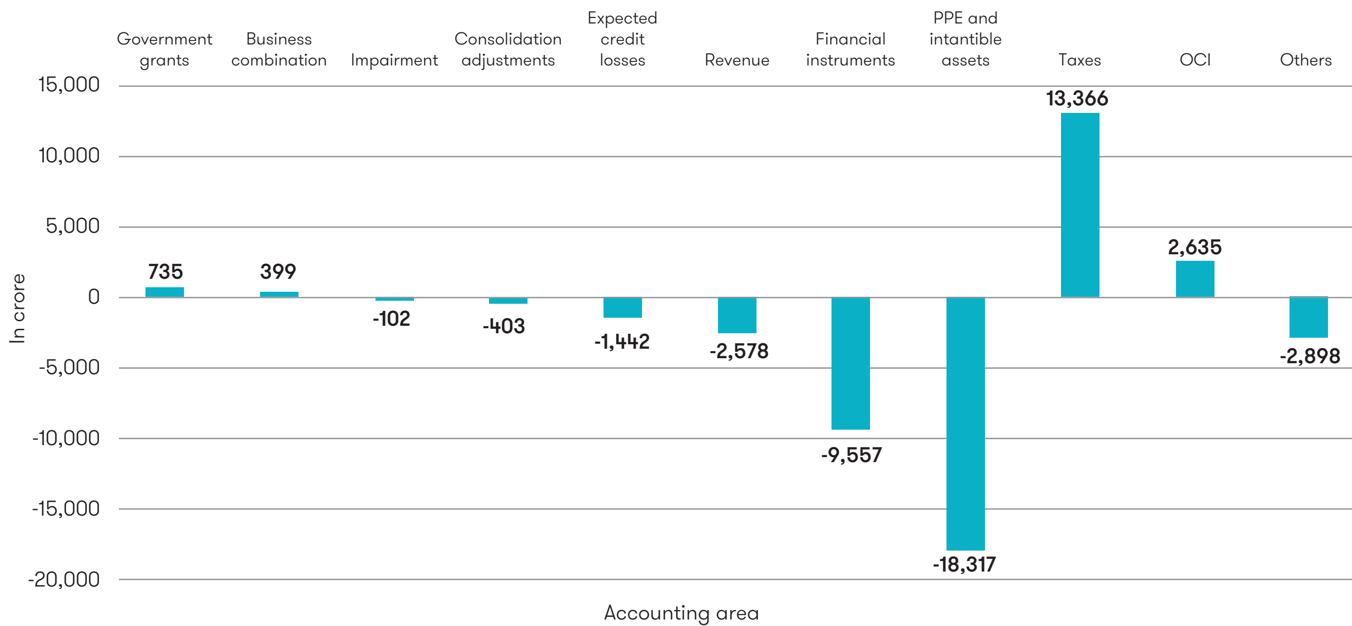
- choice of appropriate accounting policies and consistency in application thereof, across subsidiaries, segments, jurisdictions and sectors
- well-defined systems for timely and accurate financial reporting
- reliance on processes rather than on people.

Impact summary

(I) The chart below is a graphical representation of accounting area-wise aggregated Ind AS impacts reported by companies on their Equity as on 31 March 2016 reported under the previous GAAP:



(II) The chart below is a graphical representation of accounting area-wise aggregated Ind AS impact reported by companies on their total comprehensive income for the year ended 31 March 2016 reported under the previous GAAP:



Sector-wise accounting area analysis matrix

Industry /Areas	Business Combination	Expected credit losses	Revenue	Financial instruments	PPE and intantible assets	Taxes	OCI	Others
Automotive and ancillary	Medium	Medium	Medium	High	Medium	High	High	High
Construction, engineering and infrastructure	High	High	Low	High	High	High	Medium	Low
Manufacturing	Low	Medium	Low	High	High	High	High	High
Power	Medium	Low	High	Medium	Low	Low	Medium	Low
Real estate	Medium	Medium	Medium	Low	Low	Medium	Low	Medium
Telecommunication	-	Low	Medium	Medium	Low	Medium	High	Medium
Chemicals and fertilizers	Low	Low	Low	Medium	Low	Medium	Medium	Low
Information technology	Medium	Low	Low	Low	Low	Medium	High	Low
Media and entertainment	Low	Low	Medium	Low	Low	Low	Low	Medium
Oil, gas and mining	-	Medium	Medium	High	Medium	Medium	High	High
Retail	-	Low	Low	Low	Low	Low	Medium	Low
Pharma Industry	Medium	Low	Low	Medium	Medium	Medium	Low	Low
Logistics	Low	Low	High	Medium	Medium	Medium	Medium	High
Service	Low	Low	Low	Medium	Low	Medium	Medium	Medium

High Medium Low

Analysis of key impact on accounting under Ind AS: Common areas

Common areas of impact

Based on our analysis of the profit reconciliation and equity reconciliation submitted by companies in all sectors for difference between financial statements prepared under accounting standards laid down in existing Indian GAAP (or "AS Rules, 2006") and financial statements prepared under Ind AS (or "AS Rules, 2015"), we have identified few common Ind AS impact areas. The analysis below provides detailed guidance to assist readers in understanding the difference between the two GAAPs in the most common area of adjustments across all sectors:

1. Financial Instruments

With the changing landscape of Indian economy and more liberalisation, raising funds in national and international markets through different forms of instruments has gathered momentum. As companies expand their horizon, investors are getting cautious to invest through different means to achieve their intended objective, which could be fixed return like a debt instrument or a residual share in net assets like equity or both. Several type of instruments are issued like convertible preference shares, FCCBs, foreign currency loans, debt syndication arrangements, loans from group companies, etc. by borrowing entities for raising funds.

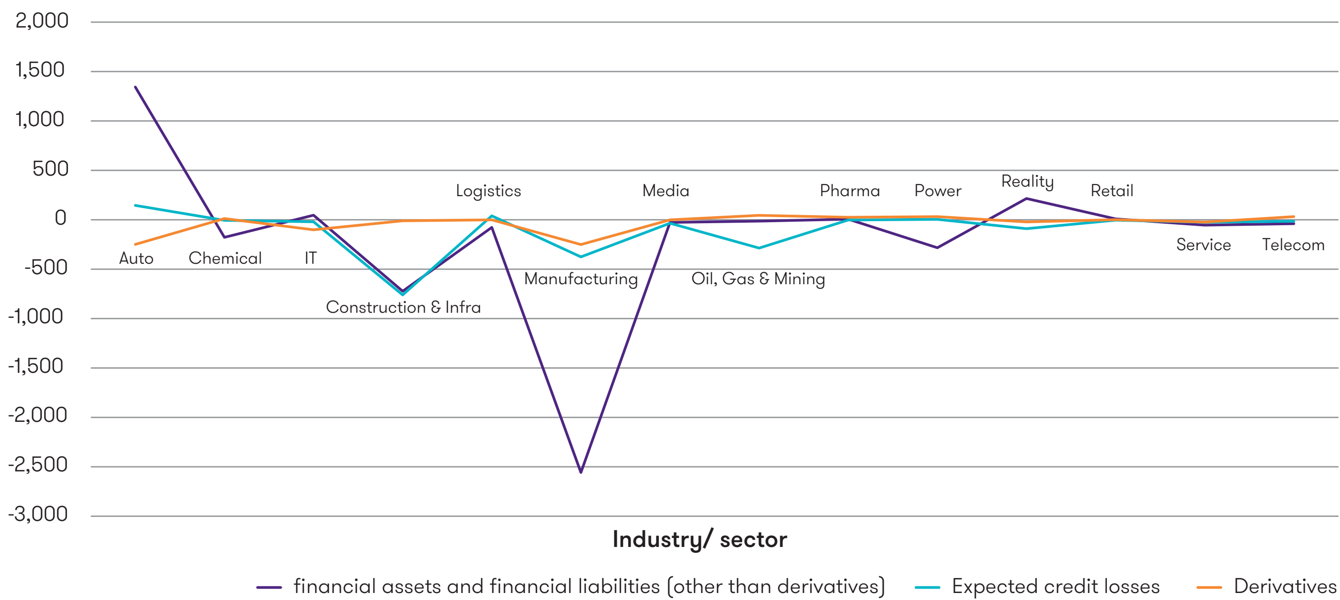
Under the existing Indian GAAP, there was no standard dealing with financial instruments. The limited guidance included – Accounting Standard 13 "Accounting for Investments" which dealt with only investments' accounting and guidance note which dealt with derivative contracts. Though ICAI had issued AS 30 "Financial Instruments: Recognition and Measurements", AS 31 "Financial Instruments: Presentation" and AS 32 "Financial Instruments: Disclosures" but those were never notified by MCA for mandatory application by Indian companies.

Under Ind AS, there is a detailed guidance on financial instruments which is covered under four accounting standards, namely –

- Ind AS 109 "Financial Instruments",
- Ind AS 32 "Financial Instruments: Presentation",
- Ind AS 107 "Financial Instruments: Disclosures", and
- Ind AS 113 "Fair Value Measurement" for accounting and disclosure of financial instruments.

Based on analysis of Ind AS financial results of more than 500 companies, the impact of accounting for financial instruments on the net profit of companies for the year ended 31 March 2016 reported under Ind AS as compared to that reported under existing Indian GAAP has been depicted in the graph below:

Financial instruments - sector-wise analysis



Certain key observations from this chart are as follows:

- Measurement of financial assets and liabilities has been an area of wide ranging impact across all sectors. While automotive sector experienced a positive impact on their net profits of close to Rs. 1,400 crore, manufacturing sector reported a decline by more than Rs. 2,500 crore.
- Impact of derivatives on profit or loss. Its likely that many corporates have applied hedge accounting in order to minimise the volatility in their reported net profits.
- Expectedly, construction and infrastructure sector has been adversely affected by the new methodology of measuring allowance for expected credit losses.

Some of the common Ind AS adjustments for financial instruments are:

a Fair valuation of financial assets
b Measurement of financial assets and liabilities at amortised cost
c Fair value of financial guarantee
d Amortisation of processing fees on borrowings (which is basically EIR)
e Fair valuation of Derivatives
f Interest accrual on preference shares (classified as liability under Ind AS)

Financial instruments are recognised when a Company becomes a party to the contractual provisions of the financial instruments and are measured initially at fair value adjusted by transactions costs, except for those carried at fair value through profit or loss which are measured initially at fair value.

Basis above definition, a financial instrument can be either of the following:

Financial asset

Common examples

- Cash
- Trade receivables
- Investments – bonds, equity instruments
- Deposits, loans receivable, etc.

or

Financial liability

Common examples

- Loans and borrowings
- Payables for purchase of goods & services
- Finance lease obligations
- Redeemable instruments like preference shares, debentures, etc.
- Guarantee given for repayment of debt upon borrower's default

or

Equity

Common examples

- Equity instruments issued
- Warrants to issue fixed number of shares at fixed price against each warrant
- Other instruments convertible into fixed number of equity shares, etc.

While all financial instruments are initially recognised at their fair value, subsequent accounting is driven by their classification in the financial statements. In turn, the classification of financial instruments is a factor of two tests –

(a) contractual cash flows test

(b) business model test, in that order.

Financial assets: Classification and measurement

For the purpose of subsequent measurement, financial assets other than those designated and effective as hedging instruments are classified as follows upon initial recognition:

- **Amortised cost** - Amortised cost instruments are initially recognised at their fair value less transaction costs and subsequently, interest is accrued on a periodical basis using effective interest method.
- **Financial assets at fair value through profit or loss (FVTPL)** – Includes financial assets that either do not meet the criteria for amortised cost classification or are instruments held for trading or that meet certain conditions and are designated as at FVTPL upon initial recognition.. Assets in this category are measured at fair value with gains or losses recognised in profit or loss.
- **Financial assets at fair value through other comprehensive income (FVOCI)** – Includes financial assets that are either debt instruments managed under hold to collect and sell business model or are non-trading equity instruments that are elected to be classified under this category.

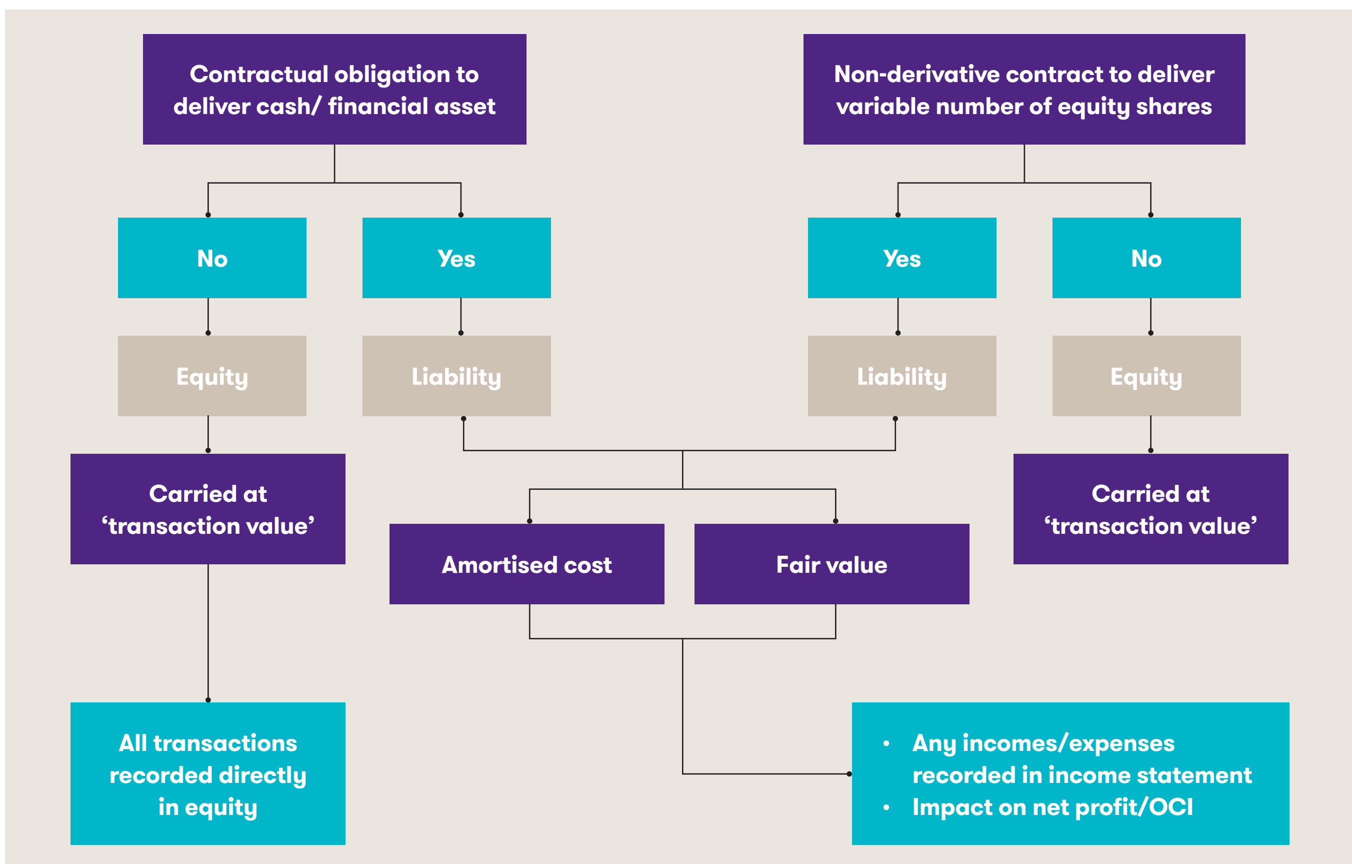
Financial liabilities – Classification and measurement

For financial liabilities, there are two measurement categories:

- **Amortised cost** – All financial liabilities are measured subsequently at amortised cost using the effective interest method except below. Amortised cost instruments are initially recognised at their fair value less transaction costs and subsequently, interest is accrued on a periodical basis using effective interest method.
- **FVTPL** – Financial liabilities held for trading or designated as FVTPL, that are carried subsequently at fair value with gains or losses recognised in profit or loss. For eg.: all derivatives (such as foreign currency forwards or interest rate swaps), or liabilities that it classifies as 'held for trading'.

Equity: Identification and distinction from financial liability

Equity represents residual interest in net assets of an entity. The distinction between financial liability and equity is extremely critical to determine accounting in the financial statements. While financial liability is initially recognised at fair value and subsequently based on its classification as mentioned above, equity instruments are carried at their transaction value. In principal, the fundamental distinction between debt and equity is explained below:



The adjustments with major impacts observed in this area are:

Interest-free or off-market interest bearing loans and advances

It is common business practice in many sectors to extend such loans and advances to related or unrelated entities. Under existing Indian GAAP, such loans are accounted for at their transaction value. However, under Ind-AS, loans and advances recoverable in cash are initially recognised at their fair value, usually represented by the present value of expected cash flows discounted at market interest rate.

The initial measurement difference between the transaction value and fair value of the financial instrument is recognised based on the underlying relationship between the lender and the borrower:

1. As an asset or liability, if that difference is representative of a separate asset or liability that qualifies for recognition under Ind AS. or an equity contribution in the books of borrower; and
2. If no asset or liability arises, then such difference is recognised in profit or loss as follows:
   a. If the fair value is evidenced by a quoted price in an active market for an identical asset or liability (ie, level 1 input) or based on valuation technique using data from observable inputs – day 1 difference is recognised in profit or loss;
   b. In all other cases, day 1 difference is deferred and recognised in profit or loss on time proportion basis. Subsequently, the financial instrument is carried at its amortised cost through recognition of interest income thereon using effective rate method. The corresponding asset/ liability that arose on initial recognition shall be amortised on a systematic basis in the income statement.

Transaction costs (like processing fees) in respect of borrowings

Under existing Indian GAAP, either companies charge off transaction costs upfront or amortise over the term of loan. Under Ind AS, most financial liabilities (including borrowings) are initially recorded at their fair value, less directly attributable cost (transaction costs). Subsequently, such borrowings are carried at their amortised cost using effective interest method; hence transaction costs are charged off in profit or loss as part of effective interest rate over the term of loan.

Investments in equity instruments

a **Fair valuation of investments** – Companies often make investments in equity instruments of investee entities that are either strategic investments in group companies (subsidiaries/ associates/ joint ventures); or other companies for purpose of earning capital gains. Under existing Indian GAAP, investments are simply classified as 'long term investments' – carried at cost unless there is a decline other than temporary in the carrying value of investments and 'current investments' – carried at lower of cost and fair value.

   Under Ind AS, all investments are initially recorded at their fair value (often represented by their transaction price) and subsequent such investments are re-measured at their fair value with gains or losses recognised in profit or loss (ideally when the intention of such investment is of trading), unless Company makes an irrevocable election upon initial recognition of such investments to recognise all fair value changes in other comprehensive income (ideally when the intention is of strategic nature). Ind AS 113 states how to compute fair value for the assets and liabilities.

b **Notional investment resulting from off-market loans** – Where companies make loans to their subsidiaries, associates or joint ventures at off-market interest rates, such loans are accounted on day 1 at their fair value, represented by future cash flows discounted to their present value using market rate of interest. Difference, thus arising on day 1 is accounted as 'investment in borrower entity' and considered as part of equity investment, which will be adjusted only upon disposal or upon impairment where carrying value is reduced to its recoverable amount.

Impairment of financial assets

Under existing Indian GAAP, provision for bad and doubtful debts is based on evaluation of past events and on consideration of information available up to the date including review of events occurring after balance sheet date; or in other words, one can say, this model is an "incurred credit loss model". Ind AS makes a significant departure from this approach and prescribes the "expected credit loss model" whereby a loss allowance for expected credit losses is recognised for certain financial assets, including those carried at amortised cost, based on expectation of events which may happen in future.

Derivative financial instruments

Under the existing Indian GAAP, where derivatives are taken for highly probable forecast transactions or firm commitments, they are marked to market at every period end with only losses being recognised and gains being ignored. If companies have taken forward instruments for existing assets/ liabilities, forward premium is amortised over the contract term. There is no notified standard which provides guidance on hedge accounting for any derivatives other than forward contracts.

Under Ind AS, all derivative instruments are carried at fair value, with MTM gains/ losses being recognised in profit or loss unless company opts for hedge accounting. Detailed guidance on how hedge accounting impacts companies has been explained in the analysis of impact of Ind AS on Pharmaceutical sector, later in this publication.

Classification as 'financial liability' or 'equity'

Ind AS 32 deals with presentation of financial instruments from Issuer's perspective – as equity or financial liability; or if both elements exist in the same instrument. Ind AS 32 prescribes substance based accounting principles and ignores the legal form of such instruments. For example - redeemable preference shares carrying cumulative (compulsory) market rate of coupon, will be classified as financial liability under Ind AS, with dividend on such instruments accounted as 'finance cost' in the income statement. Under existing Indian GAAP, the same was classified as part of 'share capital' with dividend being appropriated from reserves.

1 Due to change in classification of financial liability and equity as compared to Indian GAAP, there are significant impact seen on the debt-equity ratio.
2 This has led to companies paying attention on the financing transactions, so as to ensure that accounting evaluation is consistent with the commercial intent of such transactions.

2. Deferred Taxes

AS 22 “Accounting for Taxes on Income”, is primarily based on the income statement approach which focuses on timing differences between taxable income and accounting profit that originate in one period and are capable of reversal in one or more subsequent periods. Further, deferred tax is recognised only for timing differences and not permanent differences.

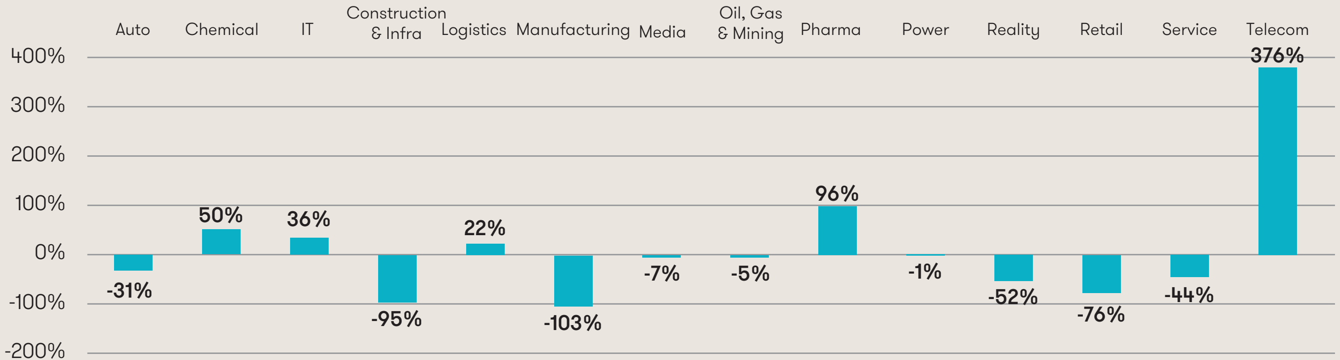
However, Ind AS 12 “Income Taxes” is based on balance sheet approach and focuses on temporary differences between the carrying amount of an asset or liability in the statement of financial position and its tax base. Temporary differences may be either:

a taxable temporary differences, which are temporary differences that will result in taxable amounts in determining taxable profit (tax loss) of future periods when the carrying amount of the asset or liability is recovered or settled; or

b deductible temporary differences, which are temporary differences that will result in amounts that are deductible in determining taxable profit (tax loss) of future periods when the carrying amount of the asset or liability is recovered or settled.

Majority of the companies which have been analysed as part of this publication have been impacted due to deferred tax adjustments, as a natural consequence of change in underlying values of assets/ liabilities in Ind AS. However, the trend of impact of tax as a percentage of total Ind AS adjustments indicates a lot of diversity and extent of impact in the recognition of taxes, largely attributable to reasons mentioned above -

Tax impact - as % of Ind AS adjustments



The above impact of deferred taxes is largely attributable to adjustment on several items that were not covered within the ambit of deferred tax in existing Indian GAAP. For instance:

- Ind AS adjustments that lead to change in carrying value of assets/ liabilities in accounting books under Ind AS with no corresponding change in the taxable value of such assets/ liabilities.
- Permanent timing differences under existing Indian GAAP where no deferred tax was recognised. For eg: revaluation of assets, or items which have been charged directly to equity, etc. Some of those differences fulfil the definition of temporary differences and hence deferred tax asset or liability is recognised.
- Deferred tax liability in consolidated financial statements 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 the timing of the reversal of the temporary difference, and it is probable that the temporary difference will not reverse in the foreseeable future.
- Further, there is deferred tax recognised in consolidated financial statements for differences between fair value of assets acquired and their carrying values in standalone books, so far as those fair value adjustments lead to temporary differences between accounting and tax base.

3. Other Comprehensive Income

Under existing Indian GAAP, companies prepare statement of profit and loss and certain specific items not recognised therein are directly recorded in reserves.

Under Ind AS, Statement of profit and loss is divided into two parts –

a Profit or loss; and
b Other Comprehensive Income - where certain specific items are presented.

Both of them combined together represent "Total Comprehensive Income". Items recognised in other comprehensive income include items that (a) can be reclassified to profit or loss and (b) cannot be reclassified to profit or loss.

Key list of certain items presented in OCI is as follows:

- Changes in revaluation surplus (existing Indian GAAP – recognised directly in revaluation reserve)
- Re-measurements of defined benefit plans (existing Indian GAAP – recognised in profit or loss)
- Gains and losses arising from translating the financial statements of a foreign operation (existing Indian GAAP – recognised directly in currency translation reserve)
- Gains and losses from investments in equity instruments/ financial assets measured at FVOCI (existing Indian GAAP – not applicable): refer section 1 above for discussion on financial instruments.
- Effective portion of gains and losses on hedging instruments in a cash flow hedge (existing Indian GAAP – certain entities which applied hedge accounting recognised directly in cash flow hedge reserve).

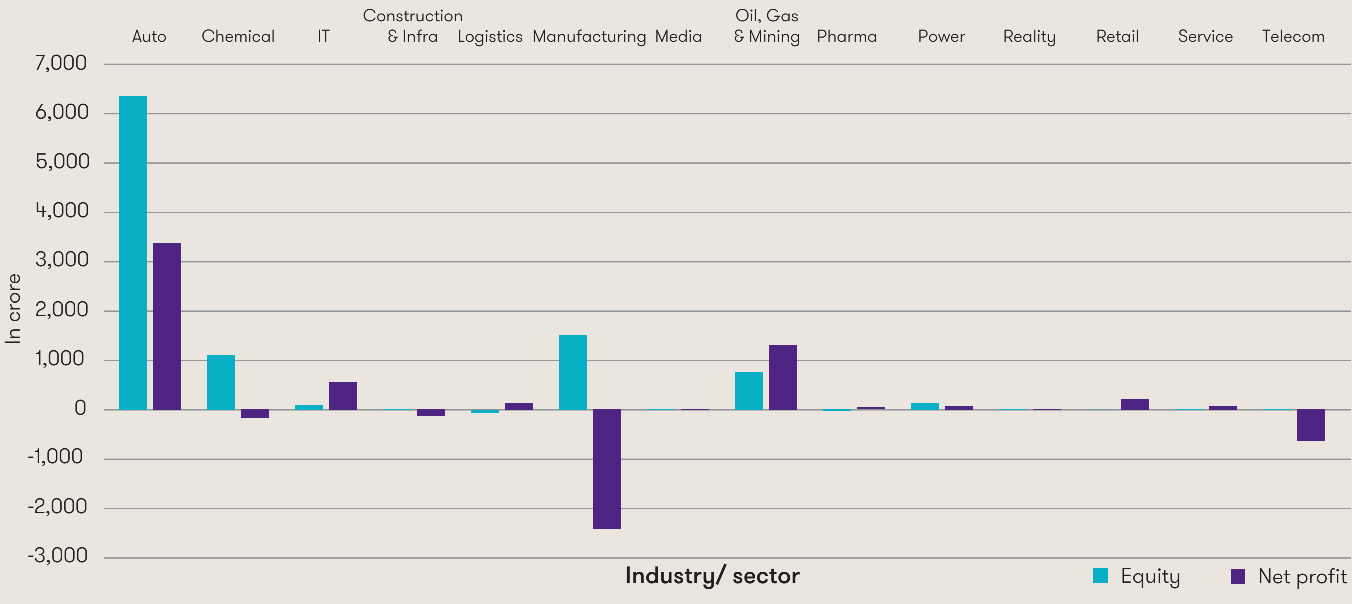
Based on analysis of annual Ind AS financial statements of over of 500 companies, some of the common adjustments in other comprehensive income include:

a Re-measurement of defined benefit plans;

b Fair value adjustments for investments designated as 'fair value through other comprehensive income'; and

c Hedging instruments designated as cash flow hedge.

The analysis of impact of all of the above on the Equity reported as at 31 march 2016 and total comprehensive income for the year ended 31 March 2016 under Ind AS compared to previous GAAP is depicted below:



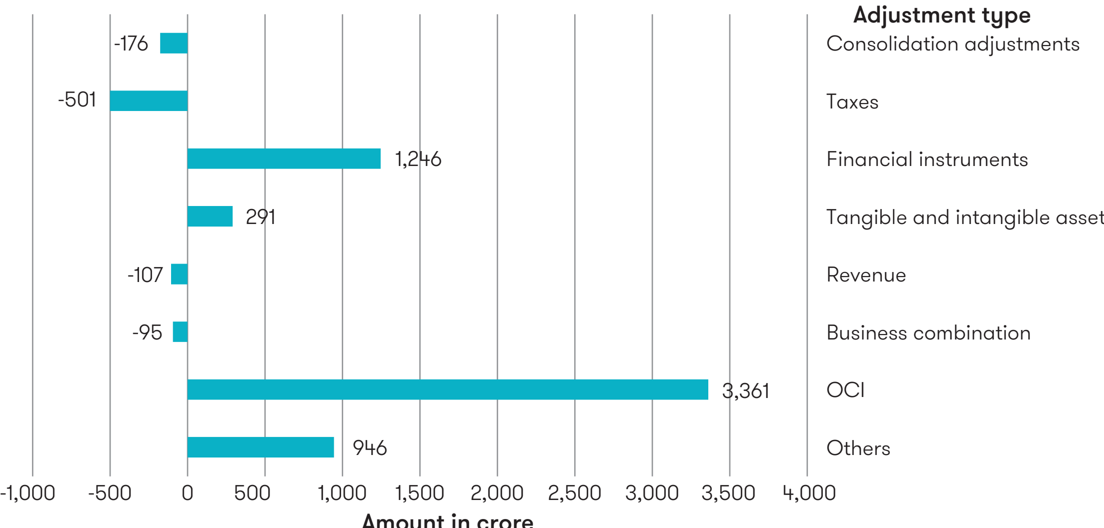
Analysis of key impact on accounting under Ind AS: Industry-wise key areas

Sector-wise analysis: Automotive and ancillaries

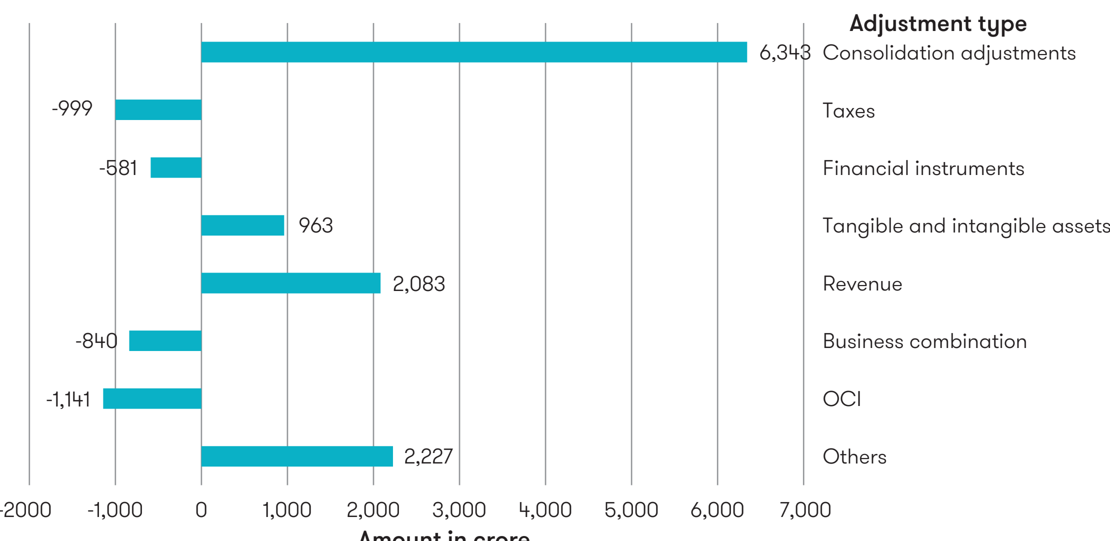
The big picture

A total of 37 listed companies in the automotive and ancillaries sector were considered for analysis of financial results prepared as per Ind AS. The charts below depict the impact of Ind AS on the net profit and equity reported by companies under Ind AS as of and for year ended 31 March 2016 as compared to previous GAAP.

Impact on total comprehensive income for FY ended 31 March 2016 under Ind AS as compared to IGAAP (Rs. crore)



Impact on Equity as at 31 March 2016 under Ind AS as compared to IGAAP (Rs. crore)



The Indian automotive industry is one of the largest in the world. India is currently the seventh largest producer in the world, second largest two-wheeler manufacturer, the largest motorcycle manufacturer and the fifth largest commercial vehicle manufacturer in the world.

This industry is typically represented by large car manufacturers and suppliers for automotive parts typically identified as – tier 1/ tier 2 suppliers. Long term arrangements between such car manufacturers and tier 1/ tier 2 suppliers, lead to accounting implications owing to their typical features such as –

- Price arrangements with discounts/incentives linked to sales
- Development of tools and moulds by the tier 1/tier 2 suppliers that are specific to every vehicle, whose economic user could be different from its legal owner
- Arrangements that do not take the legal form of a lease (in respect of machines laid for manufacturing components specific to each car manufacturer).

The key adjustments in this sector are related to property, plant & equipment, financial instruments, business combinations and revenue. Revenue is the corner stone of any industry and while in automotive industry, the impact on revenue is lower than that of the other key adjustments in this sector, however it may be interesting to understand some specific aspects of revenue recognition which are different from previous GAAP and have impacted this sector.

Revenue

Revenue is a key impact area for this sector due to existence for multiple forms of both B2B and B2C transactions. As this sector include the entire value chain of automobiles and related ancillaries, the products range from small generic components, patented model specific components and tools to complete OEM assembled automobiles.

The following discussion explains the key types of transactions and effects of Ind AS on such transactions:

Multiple element arrangements

Arrangements involving the supply of multiple goods or services at different points in time are often referred to as multiple element arrangements (MEAs). There was no accounting prescribed under the previous GAAP for MEAs, therefore such goods were accounted for at the contractual prices. For example, under previous GAAP an auto manufacturer who offered free after sales services to a customer for 2 years along with a car could recognise the entire revenue upon sale of the car. While varied practices existed even under previous GAAP, under Ind AS the requirement is to separate multiple goods and services provided under the same arrangement usually based on their relative fair values.

Most common types of MEAs in this sector include two or more of the following elements:

- automobile/ component supply
- services for installation of components
- after sales services of automobiles
- extended warranties

Since the product supply elements in this industry primarily dominate the commercial arrangements, service components are sometimes offered free of cost or at heavily discounted prices. Adoption of Ind AS requires revenue to be attributed to each separately identifiable element which has standalone value to the customer, thereby resulting in deferral of certain amounts of revenue till the services under the arrangement are rendered.

Sales return

Owing to strict quality standards and extensive testing, sales return of automotive components is very common in this industry. Therefore, mere delivery of components to the automobile manufactures or other intermediaries may not always mean a complete transfer of risk and reward for such goods. Accordingly, to comply with the requirements of Ind AS, an expectation based revenue is recognised after adjusting the probable sales return, thereby further pushing down revenue of companies in this sector.

Discount schemes and price adjustment clauses

Being a heavily marketed and advertised end product, automobiles attract customers with numerous discount schemes which are offered by manufacturers and after-market component suppliers to dealers and distributors. Some of these could be volume based or linked to other targets. Under Ind AS, such discount schemes are considered an adjustment to fair value of the consideration for sale of products, resulting in reduction of recognised revenue, at the time of sale even if the discount is not yet fructified and is estimated based on expected future activity of the dealers/distributors. Under previous GAAP, most such discount schemes were being accounted for as a part of selling and promotion expenditure after the relevant criteria were met by the dealers/distributors for availing such schemes.

The effect of an adjustment to revenue on account of discount schemes may not always be a mere re-classification from other expenses to revenue and in fact results in decrease in net profit due to adjustment in revenue even for expected value of discounts which have not yet been availed by the customer. For example, discount coupons or scratch cards, which are claimed by customers post the date of sale or on their next purchase.

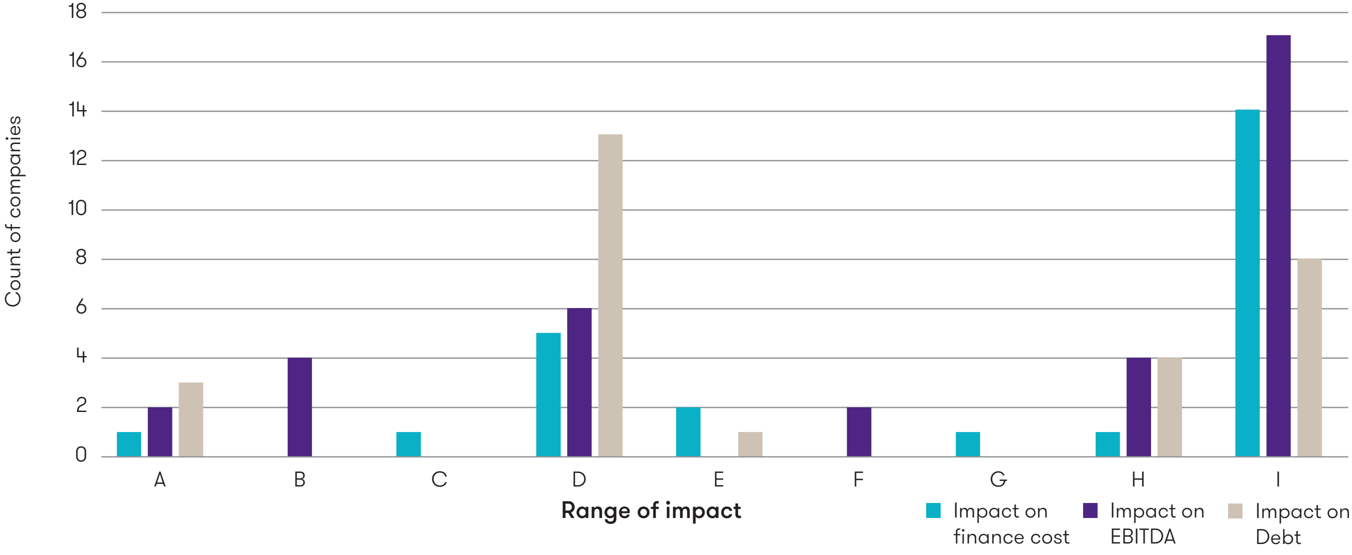
Another, common phenomenon seen in this industry is price protection clauses in contracts for sale of products, where any subsequent reductions in list price are required to be passed on to the dealers who are still holding previous stock.

Ind AS requires downward adjustment to revenue based on expectations of such reductions against such clauses.

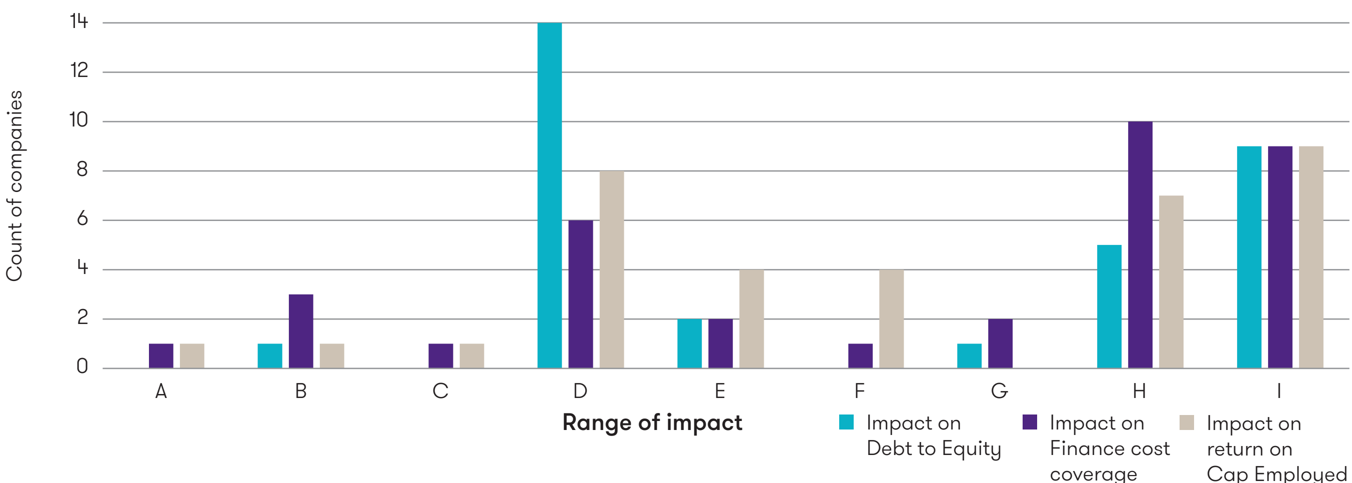
Impact upon transition:
Overall for this sector, revenue adjustments resulted in a decrease in equity of reporting companies by Rs. 840 crore, while the negative impact on net profit for the year ended 31 March 2016 is Rs. 107 crore. The impact on net profit is less than the impact on equity as it represents only an incremental impact for the year, where the opening deferred revenue is recognised in the year, positively impacting the net profit.

The charts below depict the impact on key performance metrics and ratios arising from this and other key Ind AS adjustments.

Impact on key performance metrics



Impact on key performance ratios



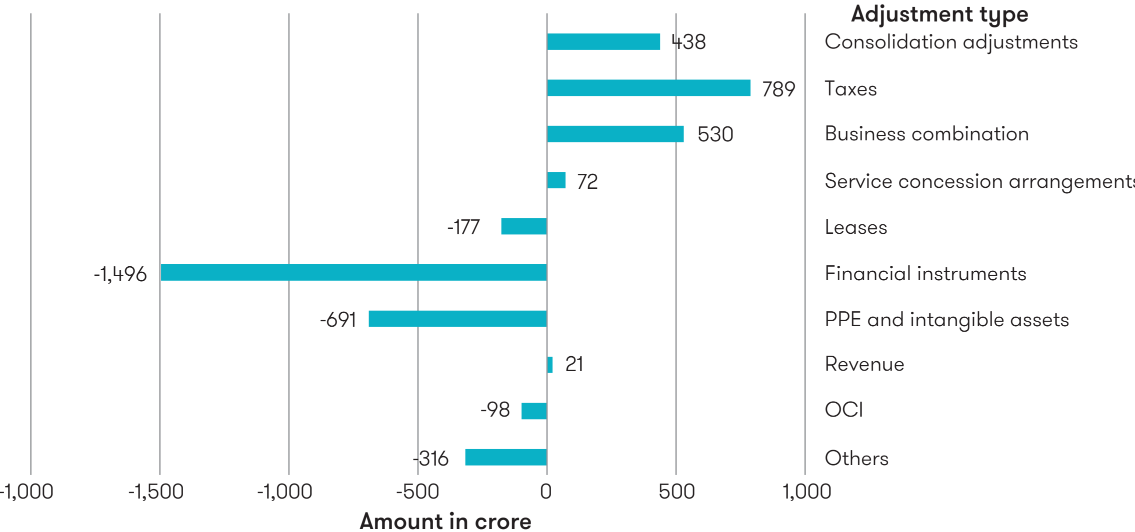
A: 5%-10% **B:** 10%-15% **C:** 15%-20% **D:** > 20% **E:** (5%)-(10%)
F: (10%)-(15%) **G:** (15%)-(20%) **H:** < (20%) **I:** (5%)-5%

Sector-wise analysis: Construction, engineering and infrastructure

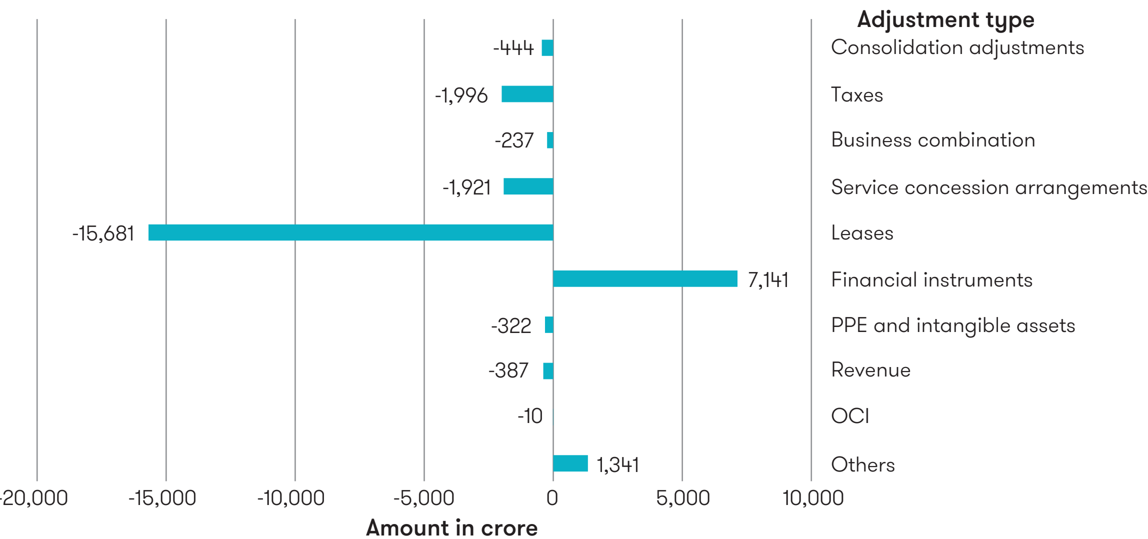
The big picture

A total of 49 listed companies in the infrastructure sector were considered for analysis of financial results prepared as per Ind AS. The charts below depict the impact of Ind AS on the net profit and equity reported by companies under Ind AS as of and for year ended 31 March 2016 as compared to previous GAAP.

Impact on total comprehensive income for FY ended 31 March 2016 under Ind AS as compared to IGAAP (Rs. crore)



Impact on Equity as at 31 March 2016 under Ind AS as compared to IGAAP (Rs. crore)



The construction industry of India is an important indicator of development and the Indian economy has witnessed considerable progress in the past few decades. The infrastructure sector also is a key contributor towards propelling India's overall development and enjoys intense focus from the government for initiating policies that would ensure time-bound creation of world class infrastructure in the country. Infrastructure sector includes power, bridges, dams, roads and urban infrastructure development.

In both the aforementioned sectors, Public Private Partnerships (PPP) are seen as a suitable medium to match the increasing demand with higher productivity and efficiency levels in the private sector. These public to private partnerships are usually executed through such arrangements, as BOOT or BOT, etc.

Further, owing to the long term arrangements entered in this industry, revenue and cost of construction have inherent unique features which attract special accounting treatment under Ind AS in comparison with existing Indian GAAP. Based on the criteria in Ind AS:

1. Such public private partnerships may result in recognition of a right to earn from operating the asset by the Operator – under Appendix A to Ind AS 11; or
2. Recognition of finance lease receivable for deemed lease of the asset by the operator to the grantor over its useful life – Appendix C to Ind AS 17. Most PPP arrangements in this sector have been accounted under this guidance.

Leases: Substance over form

The accounting treatment of leases under existing Indian GAAP and Ind AS are substantially similar, barring the guidance on arrangements that do not take legal form of a lease though in economic substance are leases. These arrangements often deal with 'right to use' of assets along with related services and are a common form of business transactions even in India. The guidance is only provided to assist in identification of leases, while the accounting treatment remains same as for legal form 'leases'.

Under the existing Indian GAAP, there is no specific guidance on determining whether an arrangement contains a lease and only the arrangements in legal form of a lease are accounted for as leases. Receipts or payments under arrangements which are not in form of a lease are generally recognised in accordance with the nature of the income or expense respectively.

Ind AS brings in detailed guidance to identify arrangement which in substance are leases or contain leases, despite these arrangements not being in legal form of a lease. The assessment whether an arrangement contains a lease depends on meeting the two main criteria, where the arrangement

- identifies a specific asset(s) to be used; and
- conveys a right to use of such asset

In line with the underlying principles of Ind AS, both these criteria are evaluated in light of substance over form. E.g. a specific asset maybe identified in the arrangement by way of being expressly specified in an agreement or implicitly in absence of a practical alternative for the seller to use in provision of services. Similarly, in determining whether there is a right to use of the asset involved, Ind AS lists down additional principles to determine whether a right to use is conveyed in the arrangement. Once a specific asset is identified and conveyance of right to use is established, the lease is accounted for under other guidance contained in Ind AS 17, which is fairly similar to the AS 19 under the existing Indian GAAP.

The practical application of the new guidance, involves multiple complexities mostly in determining whether a right to use is conveyed and sometimes for specific identification of assets too. If the arrangements that qualify to be leases under this new guidance end up being classified as finance leases, the seller/ service provider derecognises leased assets while the buyer accounts for the asset acquired under a finance lease.

If an arrangement contains a lease, then the requirement of Ind AS 17 are applied only to the lease element of the arrangement. At the inception of such arrangement, payments required by the arrangement are split into lease payments and payments related to other elements of the arrangement based on their relative fair values. In some cases, the separation of such payments will require the use of an estimation technique - e.g. with reference to a lease agreement for a comparable asset that contains no other elements or by estimating the payments for the other elements with reference to comparable agreements and then deducting these payments from total payments required. If it is impracticable to separate the lease payments, then:

1. If the lease arrangement is a finance lease, the lessee recognises an asset and a liability at an amount equal to the fair value of the asset that is identified as the subject of the lease; or
2. If the lease arrangement is an operating lease, the lessee classifies all payments as lease payments.

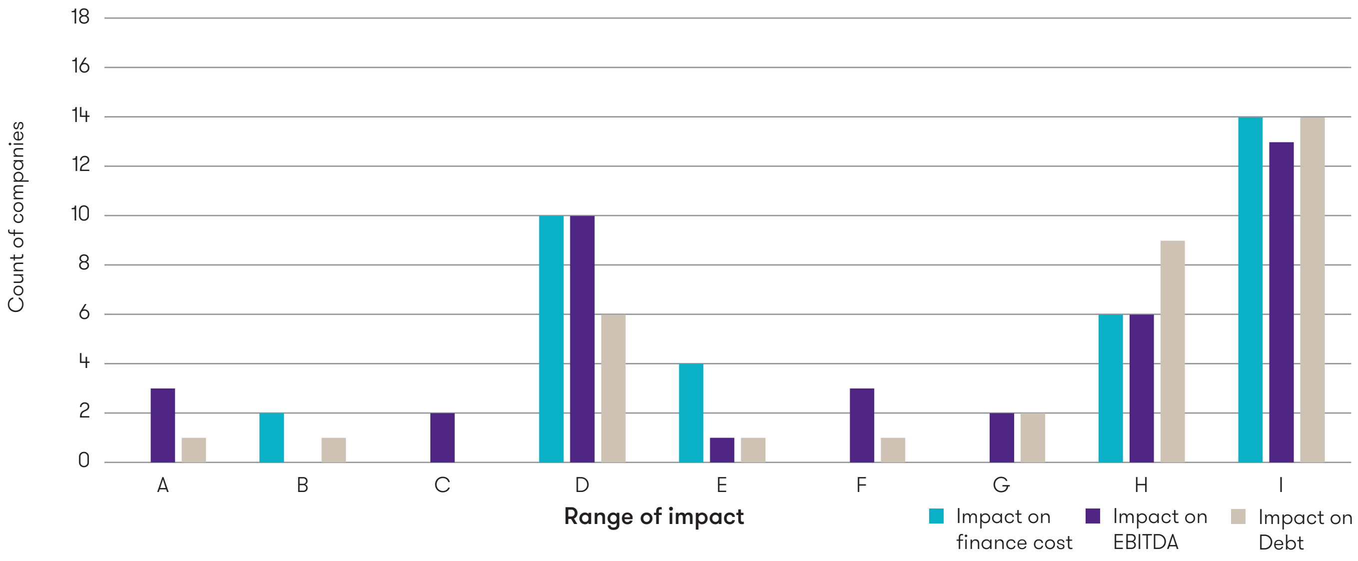
Relief upon transition:

A first-time adopter may apply Appendix C of Ind AS 17 to determine whether an arrangement existing at the date of transition to Ind ASs contains a lease on the basis of facts and circumstances existing at the date of transition to Ind AS except where the effect is expected to be not material. Therefore, an assessment of all arrangement maybe required as at the date of the transition and a retrospective assessment will not be required.

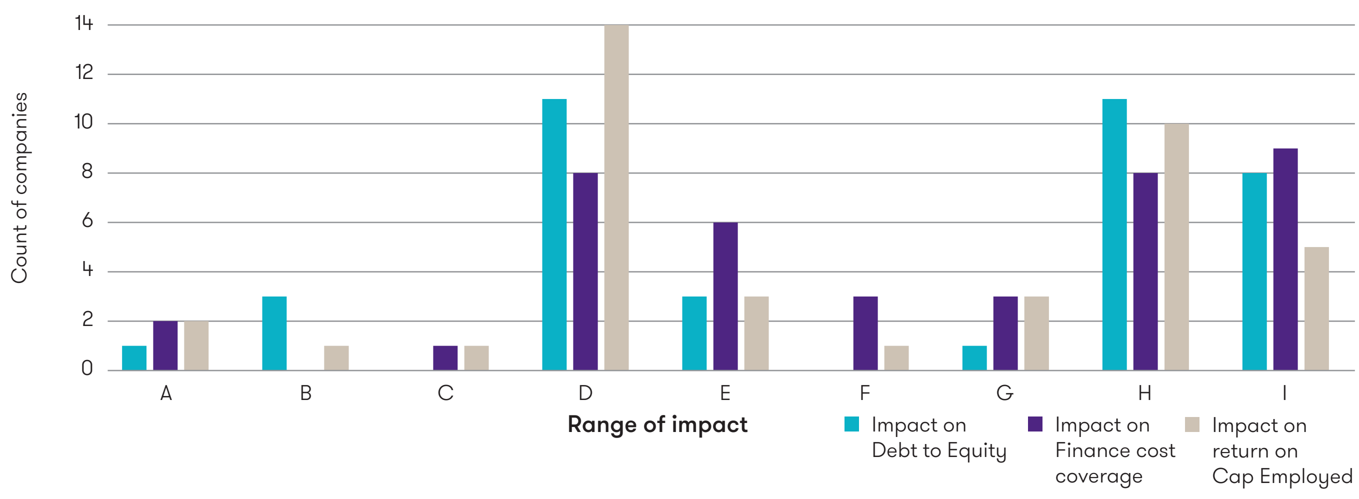
Impact on financial statements:

On account of above accounting adjustment, there is a decline of INR 177 crore on net profits with a maximum negative impact (reported by a Company in this sector) of 9% on net profit. Most companies had an impact in the range of +/-5% on EBITDA which consequently affected finance cost coverage. The charts below depict the impact on key performance metrics and ratios arising from this and other key Ind AS adjustments –

Impact on key performance metrics



Impact on key performance ratios

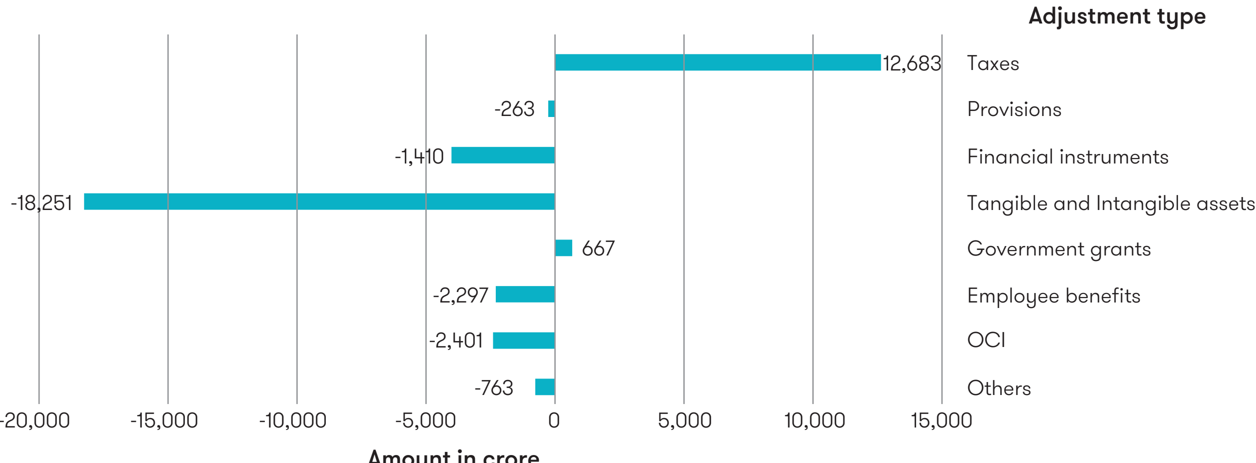


A: 5%-10% **B:** 10%-15% **C:** 15%-20% **D:** > 20% **E:** (5%)-(10%)
F: (10%)-(15%) **G:** (15%)-(20%) **H:** < (20%) **I:** (5%)-5%

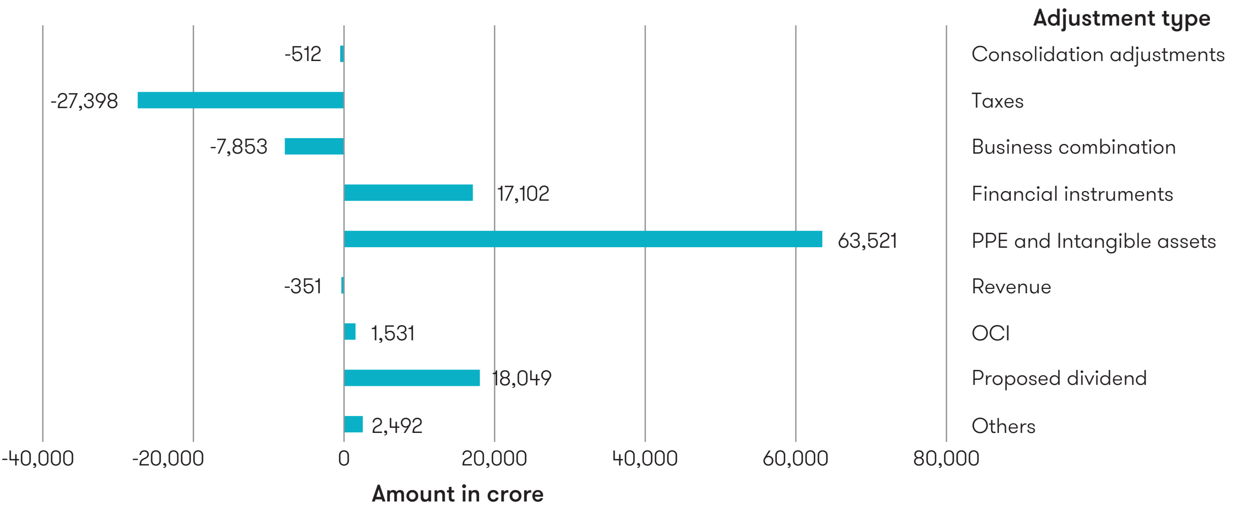
Sector-wise analysis: Manufacturing

A total of 197 listed companies, with primary business operations in this sector were considered for financial results analysis.

Impact on total comprehensive income for FY ended 31 March 2016 under Ind AS as compared to IGAAP (Rs. crore)



Impact on Equity as at 31 March 2016 under Ind AS as compared to IGAAP (Rs. crore)



Tangible assets

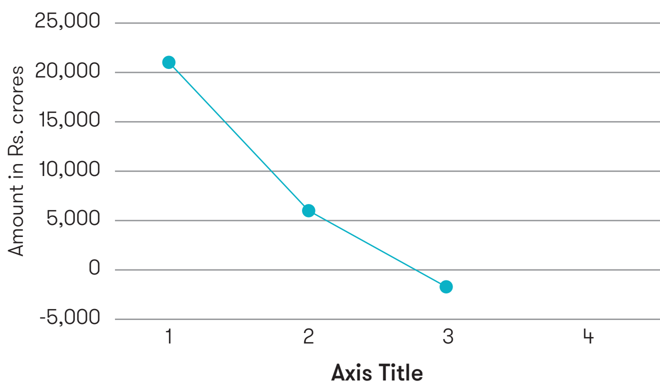
As the manufacturing sector is very capital intensive, property, plant and equipment represent the largest item on the balance sheet of these companies. Ind AS had a huge impact on the carrying value of these assets majorly because of the following adjustments:

(a) Use of fair value as deemed cost on the transition date

Ind AS 101 allows an entity to elect to measure an item of Property, plant and equipment (PPE) and Intangible assets (IA) at the date of transition at fair value and use that fair value as its deemed cost at that date. 33 companies in this sector have opted for this exemption at the transition date and have fair valued their PPE and IA resulting in a total increase of Rs. 65,614 crore in equity of these companies as of 31 March 2016. When companies avail such option for any items of PPE and/ or IA, companies need to account for other assets applying the guidance in Ind AS. To carry other assets at carrying amount as 'deemed cost' is not an option!

This option availed by a significant number of companies in manufacturing and even in other sectors, largely facilitates optimising the book value to represent the recoverable value of such assets, typically for non-depreciable assets whose book values may more often than not be outdated.

Maximum and minimum impact



Impact upon transition

As evident from the graph, the impact of fair value as deemed cost exemption has been massive for some companies and insignificant for others on equity. However, the average impact was only to the tune of Rs. 5,900 crore approx. with maximum impact reported at Rs. 21,000 crore approx. & minimum impact at Rs. (1,700) crore.

Correspondingly, this has an impact on depreciation (where fair value is opted as deemed cost for depreciable assets). From the analysis of the impact on profit –

- It appears that the larger increase in fair value was largely attributable to non-depreciable assets, while depreciable assets had a lower fair value than carrying amounts. Such adjustment has instead had favorable impact on profits, by reducing depreciation charge in subsequent periods.
- The impact of reduction of depreciation was Rs. 18,666 crore for this sector.

(b) Capitalisation of stores and spares

Ind AS requires items such as spare parts, stand-by equipment and servicing equipment to be recognised as PPE when they meet the definition thereof as per Ind AS 16. Otherwise, such items are classified as inventory. PPE are tangible items that:

a are held for use in the production or supply of goods or services, for rental to others, or for administrative purposes; and

b are expected to be used during more than one period.

About 18 companies in this sector have had an impact of this adjustment, i.e. capitalisation of stores & spares, which otherwise were charged off to consumption, thereby leading to an increase in profits by Rs. 252 crore.

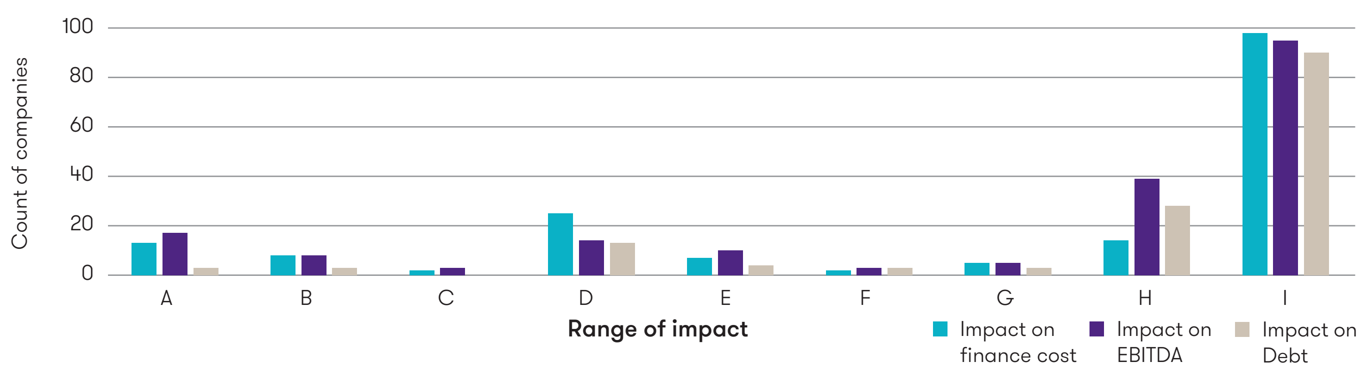
(c) Asset retirement obligation (ARO)

Under Ind AS, the discounted present value of the estimated costs of dismantling or removing and restoring the site on which an item of PPE is located is capitalised to the value of that item. A corresponding provision for ARO is also recognised at the discounted value of expected net cash outflows. The resulting additional depreciable amount of the asset is depreciated over its useful life. The periodic unwinding of the discount shall be recognised in profit or loss as finance cost as it occurs. Capitalisation of such finance cost is not permitted.

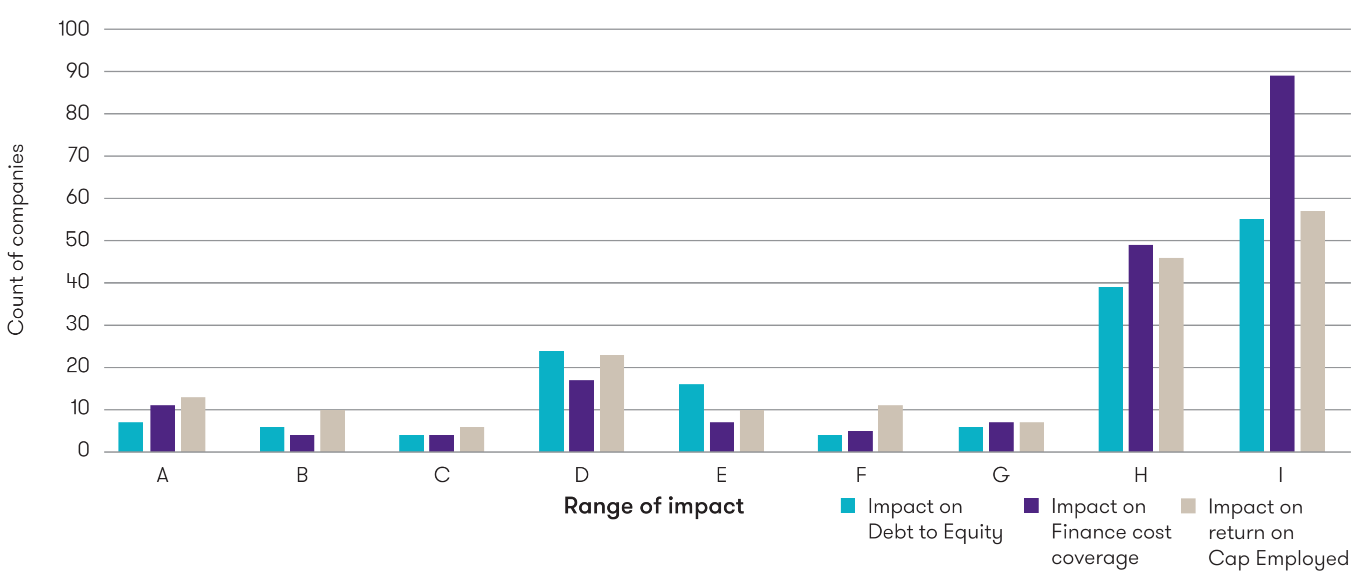
Therefore, various performance ratios like Return on Capital employed and Debt to equity are showing a slight downward trend because of the increase in equity and decrease in Profit before tax on account of increased depreciation due to the above adjustments.

The charts below depict the impact on key performance metrics and ratios arising from this and other key Ind AS adjustments

Impact on key performance metrics



Impact on key performance ratios



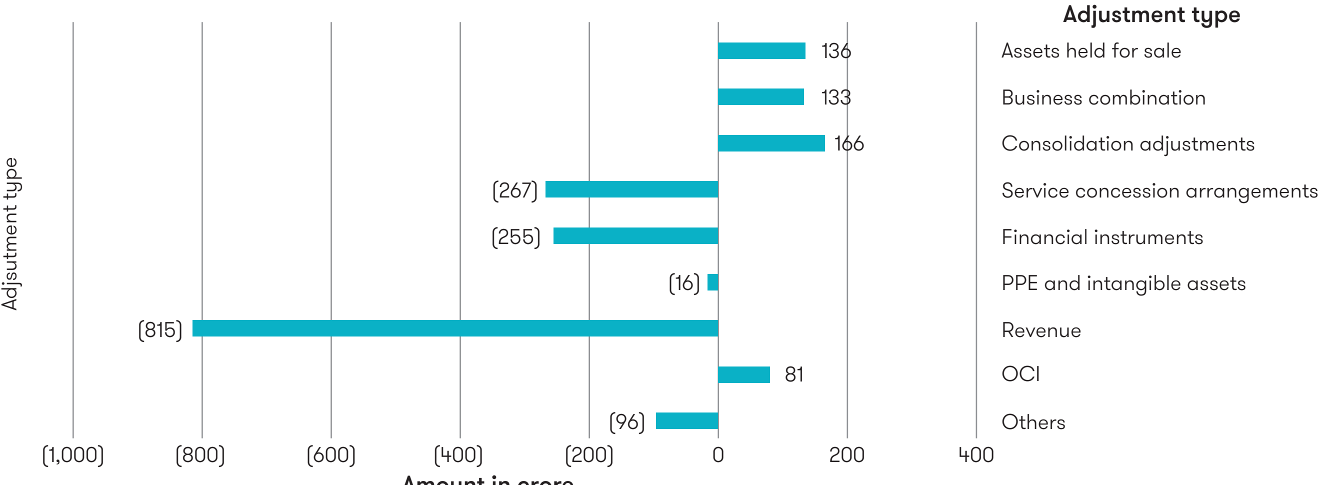
A: 5%-10% **B:** 10%-15% **C:** 15%-20% **D:** > 20% **E:** (5%)-(10%)
F: (10%)-(15%) **G:** (15%)-(20%) **H:** < (20%) **I:** (5%)-5%

Sector-wise analysis: Power

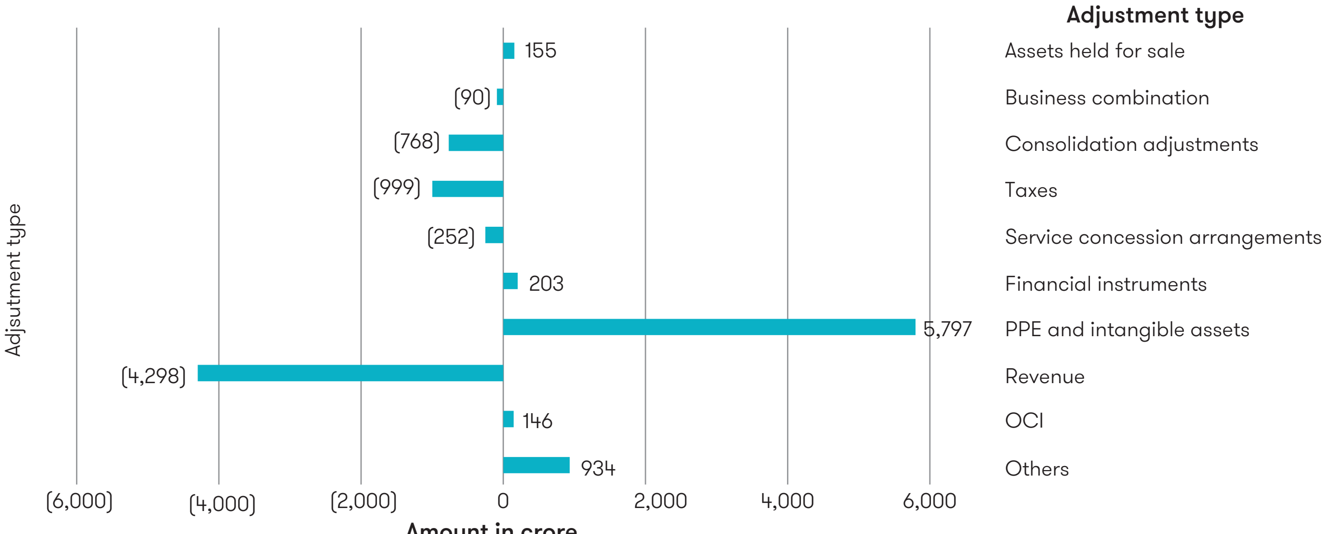
The big picture

A total of 23 listed companies, with primary business operations in this sector were considered for financial results analysis.

Impact on total comprehensive income for FY ended 31 March 2016 under Ind AS as compared to IGAAP (Rs. crore)



Impact on Equity as at 31 March 2016 under Ind AS as compared to IGAAP (Rs. crore)



Power is one of the most important and critical infrastructural constituents for any industry and thereby plays a large role in contributing to sustainable growth and development of the Economy. India is world's 6th largest energy consumer, accounting for 3.4% of global energy consumption, with Maharashtra as the leading electricity generator among Indian states.

There are three pillars of power sector – Generation, Transmission and Distribution. While public sector owns and operates nearly 2/3rd of the total power generated in the country, the remaining 1/3rd comprises private sector operators. Also, Public Private Partnerships ('PPP') are very common in this industry for generation, operation and/ or maintenance and is expected to have a noticeable impact on the accounting of infrastructural assets by the private sector. The peculiar aspects of accounting for such transactions which has impacted this industry are explained below.

Service concession arrangements

Ind AS brings in detailed guidance to identify arrangements which meet qualifying criteria of Service Concession Arrangements (SCAs). Two key conditions for any SCA to be within the scope of Appendix A to Ind AS 11 are as follows:

a Grantor, usually the Government, controls or regulates what services the operator must provide with the infrastructure, to whom it must provide them, and at what price. These terms, in substance, are usually controlled through the agreement between the grantor and the private operator.

b An evidence of government's control over any significant residual interest in the infrastructure at the end of the term of the SCA. This condition is usually met when the government obtains the ownership or beneficial entitlement of the infrastructure at the end of the term.

Where a contract falls within the scope of this guidance, they are accounted as follows:

- SCAs within the scope of the guidance are treated as 'construction' contracts, where the private operator, in capacity of a construction contractor, builds infrastructure for the government. This construction service is accounted for by the private operator at fair value and recognised as revenue, generally using the percentage of completion method. The revenue so recorded at fair value, which can be called 'accounting revenue' is recoverable and represented by right to operate and charge users over a 20-30 years' tenure.
- The right to receive money for building and operating the infrastructure could be an unconditional right, i.e. where an SCA defines a fixed amount to be charged irrespective of the use of the infrastructure, e.g. fixed capacity charges that are recovered regardless of how much power is generated and sold.
  1. In cases of such unconditional rights, the accounting asset is recognised as a financial asset and accounted in a manner similar to a loan receivable i.e. at the present value of expected net cash flows, with interest income recognised over the life of the SCA.
  2. In other cases, where the right to charge the users of the infrastructure is linked to the actual usage, a 'right to charge' intangible asset is recorded corresponding to the 'accounting revenue' and amortised over the life of the SCA.

Relief upon first time transition

Upon first time transition, where it is impracticable for an operator to apply this guidance retrospectively, the entity shall recognise financial asset/intangible asset based on the nature of arrangement as explained in the guidance above and use previous GAAP's carrying amount of those financial assets/ intangible assets, irrespective of the previous classification of such assets in previous GAAP.

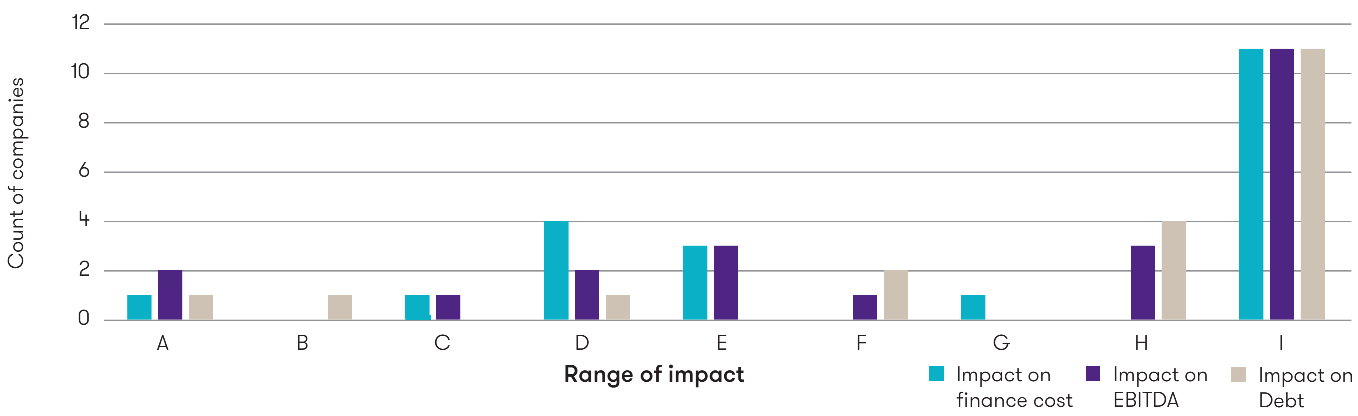
Impact on financial statements

On account of above accounting adjustment, there is an increase of Rs. 267 crore in net profit and negative impact of Rs. 252 crore in equity as of and for year ended 31 March 2016. Based on analysis of the data –

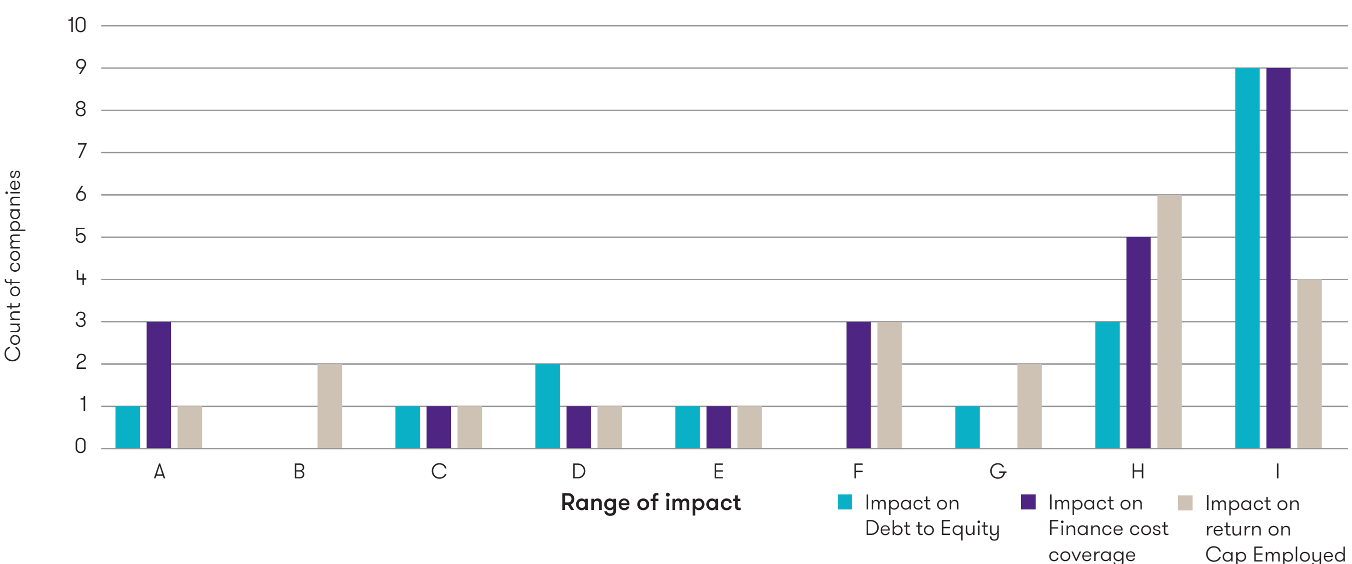
- One company reported a negative adjustment in its equity on account of service concession arrangement, which seems to suggest an adjustment in depreciation rate of the intangible asset accounted under SCA in comparison to lower depreciation rate of the property, plant & equipment accounted under previous GAAP.
- However, most other companies that accounted for service concession arrangements had a positive impact on their equity (with increase in value of intangible asset or financial receivable) and corresponding decrease in profit with enhanced amortisation of such asset.

Further, most companies had an impact in the range of +/-5% on EBITDA including impact of this adjustment on finance cost coverage. The charts below depict the impact on key performance metrics and ratios arising from this and other key Ind AS adjustments –

Impact on key performance metrics



Impact on key performance ratios

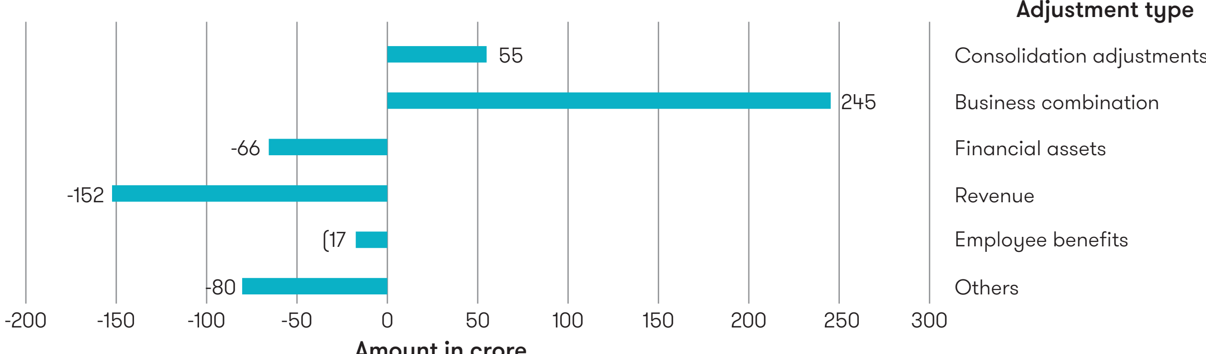


A: 5%-10% **B:** 10%-15% **C:** 15%-20% **D:** > 20% **E:** (5%)-(10%)
F: (10%)-(15%) **G:** (15%)-(20%) **H:** < (20%) **I:** (5%)-5%

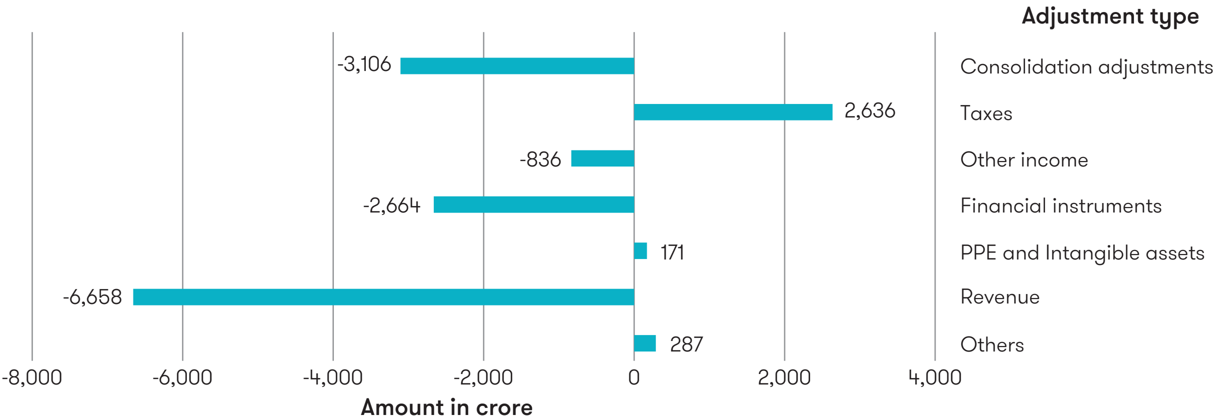
Sector-wise analysis: Real Estate

A total of 23 listed companies, with primary business operations in this sector were considered for financial results analysis.

Impact on total comprehensive income for FY ended 31 March 2016 under Ind AS as compared to IGAAP (Rs. crore)



Impact on Equity as at 31 March 2016 under Ind AS as compared to IGAAP (Rs. crore)



Real estate sector is one of the most globally recognised sectors. In India, real estate is the second largest employer after agriculture. The housing sector alone contributes 5-6 percent to the country's Gross Domestic Product (GDP). As companies in this sector are expanding, offering multiple schemes to attract customers or getting into joint development arrangements to maximise returns with optimum level of investments, such arrangements often have accounting implications in areas of revenue recognition, financial instruments, etc.

Considering revenue recognition in the real estate sector is peculiar owing to the nature of industry, the Institute of Chartered Accountants of India (ICAI) had issued a Guidance Note (GN) in the year 2012, namely 'Guidance Note on Accounting for Real

Estate Transactions (GN on Real Estate)'. With the notification of Ind AS, a need was felt to issue a new version of this Guidance Note to make accounting consistent for real estate transactions.

We have analysed the guidance under Ind AS below and how it has impacted the financial results and financial position of companies in this sector.

Revenue recognition

For real estate development, under previous GAAP, revenue was recognised in accordance with Guidance Note on Accounting for Real Estate Transactions [GN(A)23 (Revised 2012)] issued by Institute of Chartered Accountants of India (ICAI). Revenue in respect of projects commenced before 1 April 2012 was recognised in accordance with Guidance note on Recognition of Revenue by Real Estate Developers [GN(A) 23 (Issued 2006)] issued by ICAI. The 2012 guidance note requires project revenue to be measured at "consideration received or receivable " whereas the 2006 Guidance Note only provided guidance on timing of recognition of revenue.

Upon introduction of Indian Accounting Standards, a new guidance note for revenue recognition was issued by the ICAI, providing guidance for both timing and measurement of revenue recognition. Measurement of revenue draws guidance from Ind AS 18 – Revenue and Ind AS 11 – Construction Contracts which require revenue to be measured at fair value of the consideration received or receivable.

A few transactions, specific to the real estate sector, are dealt with as below:

- Where companies offer incentives or other deductions to customers, revenue is recognised at fair value and any such amounts payable to customers are estimated at the time of recognising revenue and netted off from revenue.
- Any delayed delivery compensation is considered as an adjustment to sales price when such estimate can be measured reliably and accounted as a reduction of the transaction price. If the consideration payable to a customer includes a variable amount, an entity shall make estimates and revise as & when required.

As referred above, measurement of project revenues is affected by a variety of uncertainties that depend on the outcome of future events. The estimates often need revision as events occur and uncertainties are resolved. The percentage of completion method is applied on a cumulative basis in each reporting period to the current estimates of project revenues and project costs. Therefore, the effect of a change in the estimate of project costs, or the effect of a change in the estimate of the outcome of a project, is accounted for as a change in accounting estimate. The changed estimates are used in determination of the amount of revenue and expenses recognised in the statement of profit and loss in the period in which the change is made and in subsequent periods.

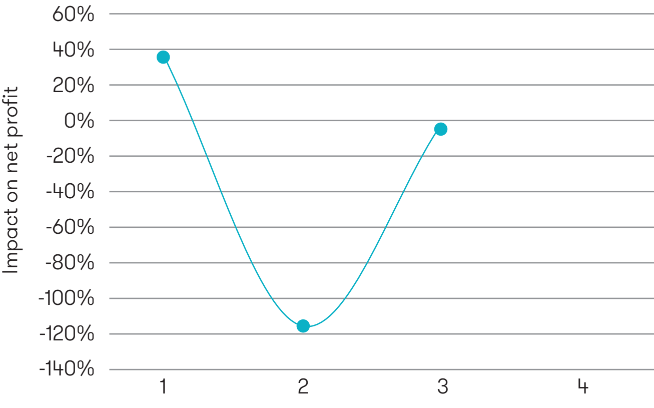
Impact on financial statements

The impact of accounting for such adjustments has resulted in reduction in revenue, thereby impacting equity by Rs. 6,658 crore and net profit by Rs. 152 crore as of and for year ended 31 March 2016. However, as evident from the graph below:

- Maximum impact was increase in net profit by 35% and minimum impact was decrease in net profit by 118% on account of revenue adjustment
- However, the average impact was approx. 4-5% for a wider range of companies.

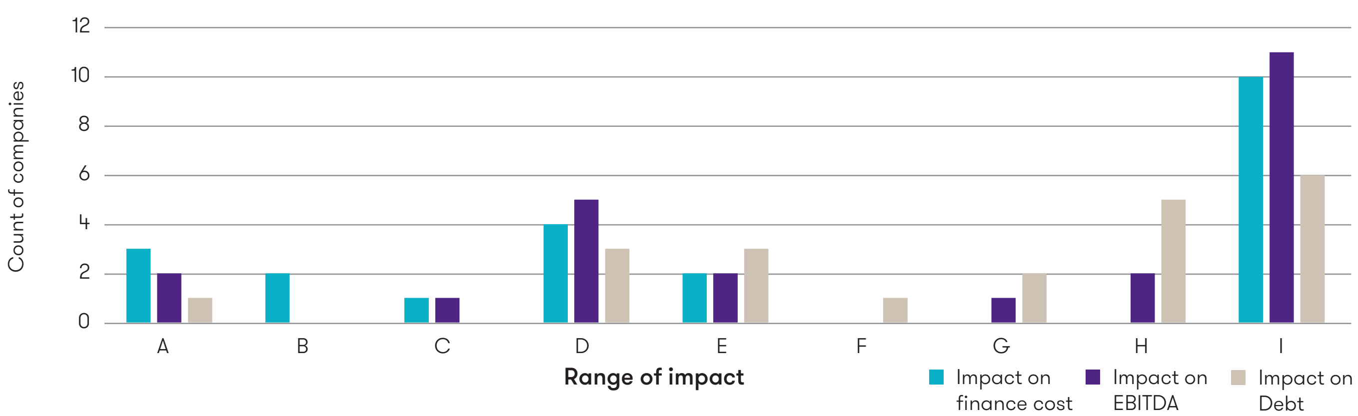
With revenue impact of nearly 4-5%, the corresponding impact was on related key performance ratios like interest coverage, return on capital employed which changed by approx. +/-5% for most companies.

Maximum and minimum impact

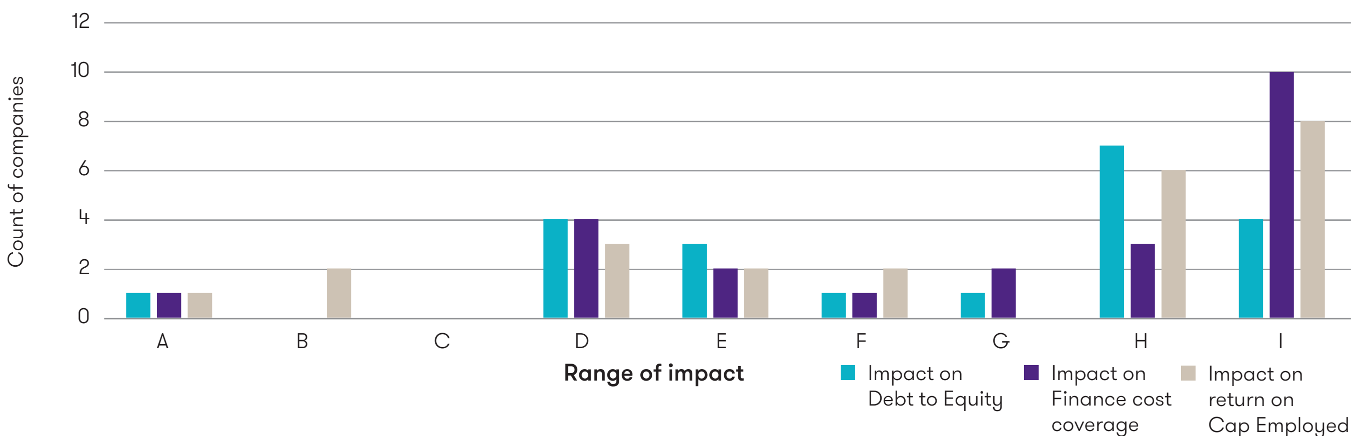


The range of impact for companies in this sector on certain key performance metrics and ratios has been depicted below:

Impact on key performance metrics



Impact on key performance ratios



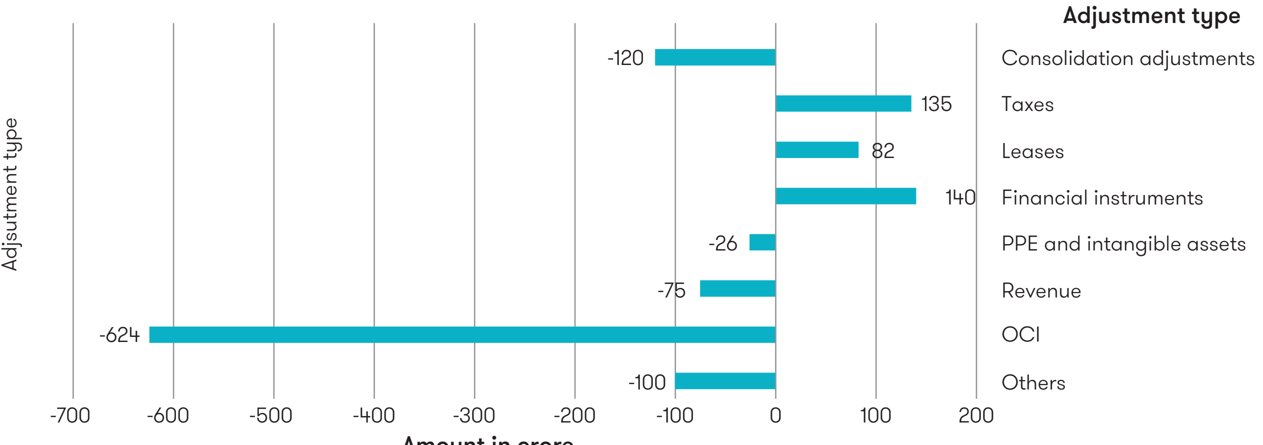
A: 5%-10% **B:** 10%-15% **C:** 15%-20% **D:** > 20% **E:** (5%)-(10%)
F: (10%)-(15%) **G:** (15%)-(20%) **H:** < (20%) **I:** (5%)-5%

Sector-wise analysis: Telecommunications

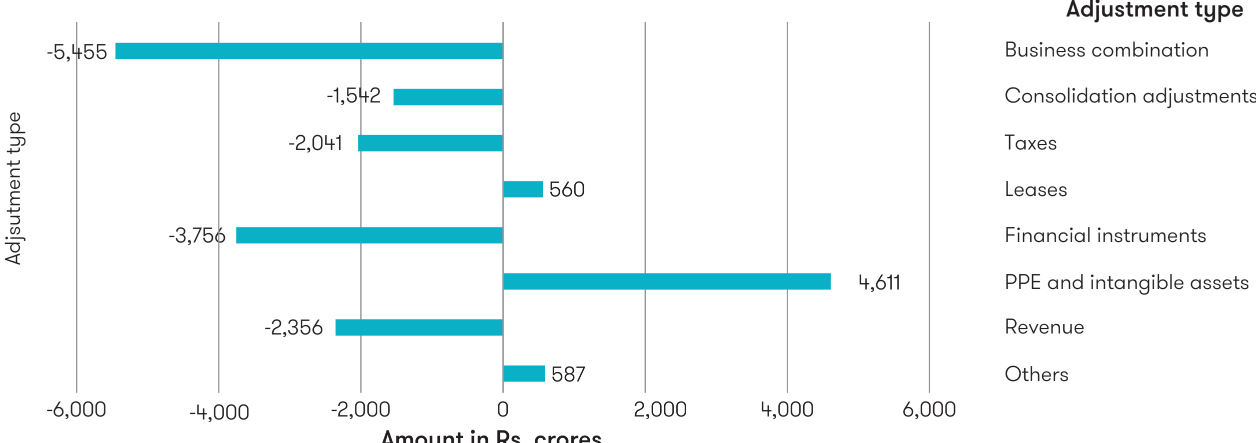
The big picture

A total of 9 listed companies, with primary business operations in this sector were considered for financial results analysis.

Impact on total comprehensive income for FY ended 31 March 2016 under Ind AS as compared to IGAAP (Rs. crore)



Impact on Equity as at 31 March 2016 under Ind AS as compared to IGAAP (Rs. crore)



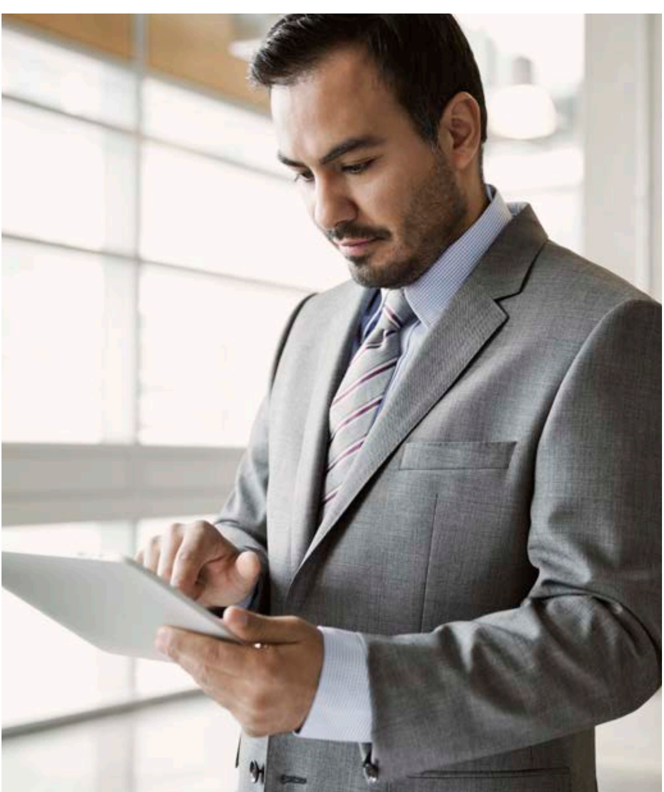
India is currently the world's second-largest telecommunications market and has registered strong growth in the past two decades. The Indian wireless communication sector is growing rapidly and is expected to contribute substantially to India's Gross Domestic Product (GDP). Many companies in this sector directly provide services to end users, and therefore discounts and incentive schemes are a common phenomenon. Under Ind AS, such schemes may need evaluation for measurement of revenue. Another common transaction in this sector is the bundling of hardware and services elements together in a single contract, where Ind

AS may require re-looking at allocation of revenue between the two components. Barter transactions between telecom providers are also not uncommon in this sector, where under Ind AS an evaluation may be necessary for gross or net revenue presentation.

Some of the key aspects of revenue recognition in telecom sector have been analysed below:

Revenue recognition and measurement: Multiple element arrangements

Companies in the telecommunication sector charge certain activation/ one-time registration charges from customers upon sale of prepaid calling card or post-paid connections. In form, such charges are attributable to one-time costs incurred by the telecom service provider for connecting the subscriber to its network. Under the contract for telecommunication services, besides the provision of the network connection, the service provider is also obligated to provide on-going telecommunication services throughout the contract period. In such cases, the connection service and the on-going telecommunications services have to be analysed in accordance with their economic substance in order to determine whether they should be combined or segmented for revenue recognition purposes.



Under Ind AS 18, the recognition criteria 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. In this sector, activation of the SIM is mandatory to provide the subscriber access to the network for any kind of service provided to the subscribers on an ongoing basis. Companies need to evaluate if a specific service can be identified separately to which the upfront activation/ installation charges can be attributed. If the answer is in the negative, some or all of such charges are considered to be an advance against telecommunication services to be provided on an ongoing basis and accordingly deferred over the customer relationship period.

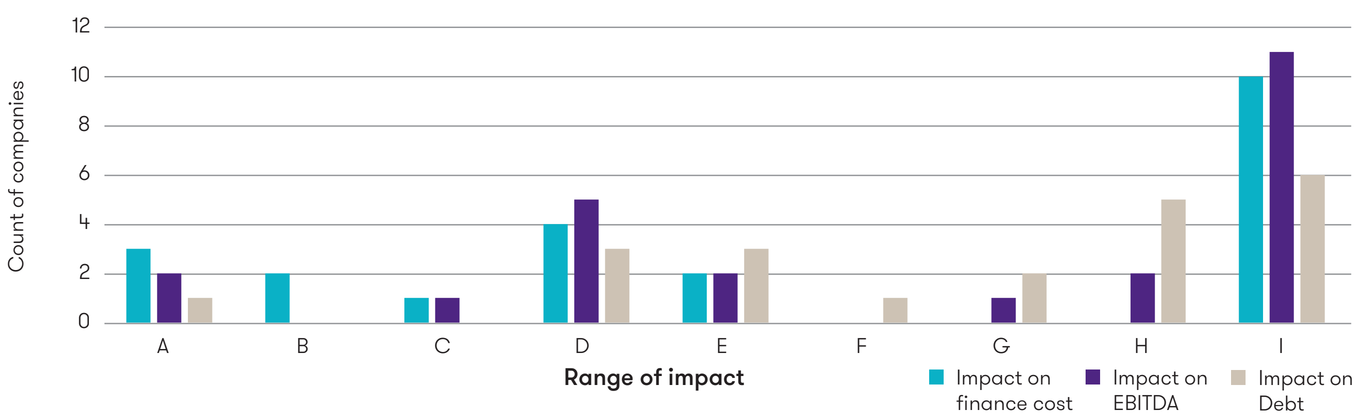
There are other forms of multiple element arrangements also which may necessitate accounting for each individually identifiable element, for instance provision of hardware (mobile handset, for instance) and services, where delivery of hardware may be segregated from the service element and recognised as and when the respective performance obligations are met.

Impact on financial statements

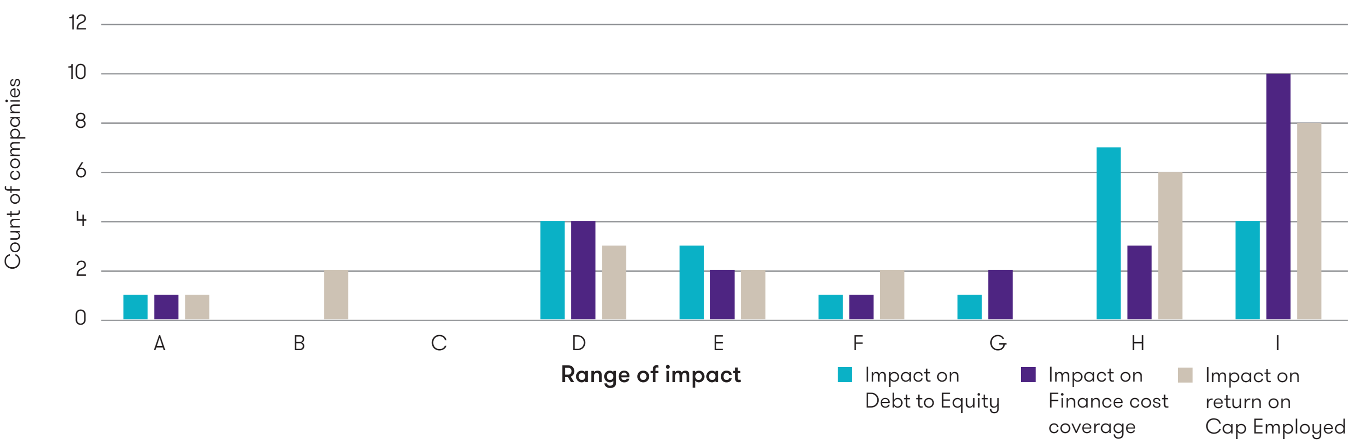
Deferral of revenue for future performance obligations is one of the most common adjustments in this sector, which resulted in an impact of Rs. 2,356 crore on the equity as of 31 March 2016. These adjustments are likely to impact EBITDA and hence, some of the key performance ratios like finance cost coverage and return on capital employed on an ongoing basis.

The range of impact for companies in this sector on certain key performance metrics and ratios has been depicted below:

Impact on key performance metrics



Impact on key performance ratios



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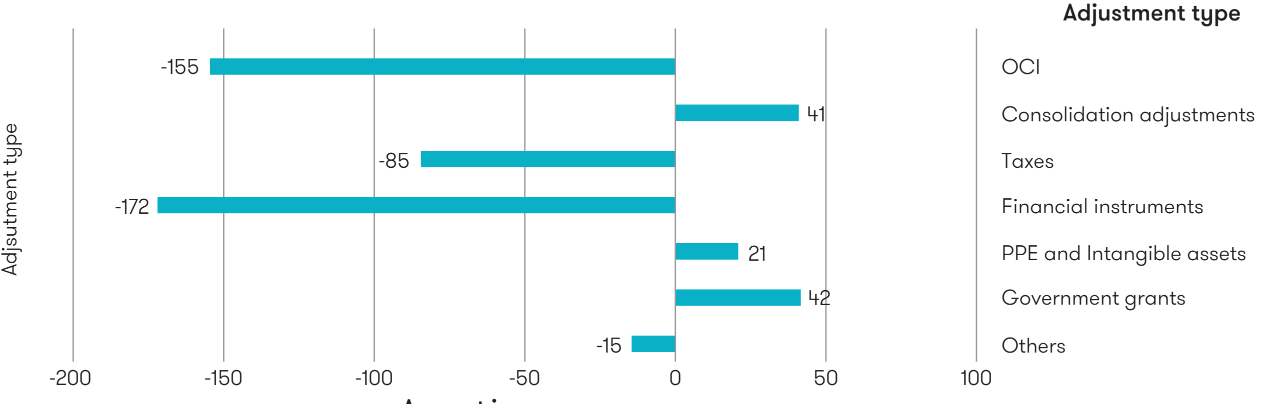
F: (10%)-(15%) **G:** (15%)-(20%) **H:** < (20%) **I:** (5%)-5%

Sector-wise analysis: Chemicals

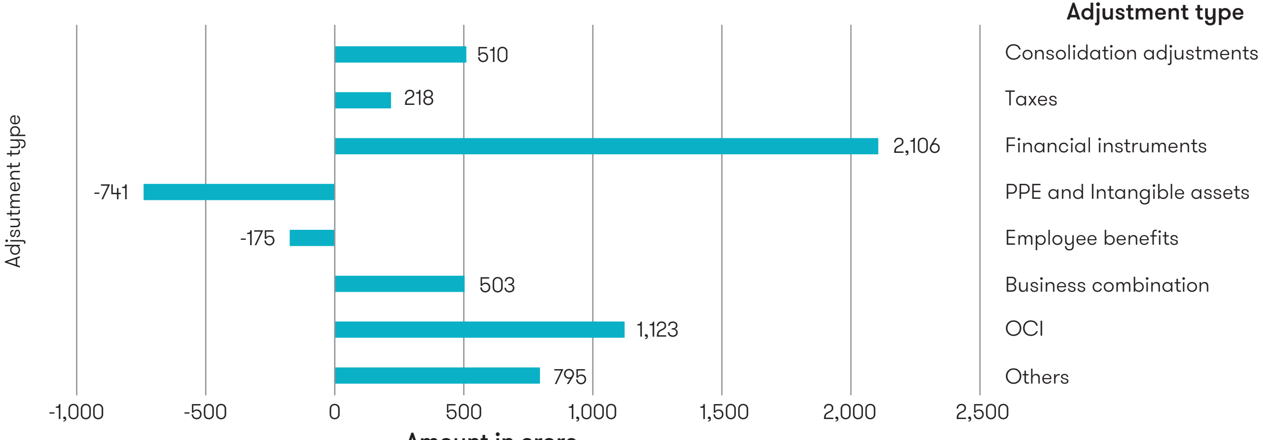
The big picture

A total of 37 listed companies, with primary business operations in this sector were considered for financial results analysis.

Impact on total comprehensive income for FY ended 31 March 2016 under Ind AS as compared to IGAAP (Rs. crore)



Impact on Equity as at 31 March 2016 under Ind AS as compared to IGAAP (Rs. crore)



The chemical sector has witnessed incredible growth in the last 5 to 7 years. The major growth drivers behind India's chemical industry are (a) growing disposable incomes and increasing urbanisation are fuelling the demand for paints, textiles, adhesives and construction materials, which, in turn, leads to substantial growth opportunity for chemical manufacturers; and (b) diversified manufacturing base that produces world-class products. Chemicals constitute contribution reasonable share of India's total exports as well.

The key adjustments in this sector that have contributed to the change in net profit and net equity under Ind AS from erstwhile Indian GAAP comprise – accounting for financial instruments (including expected credit losses), adjustments pertaining to tangible and intangible assets and government grants. The adjustment for government grants which typically has impacted fewer industries, with chemical being one of the prime ones has been discussed in detail below.

Accounting for government grants

Under the previous GAAP, grants were categorised into the following:

- Asset related grant
- Income related grant
- Grants in the nature of promoter's contribution

Under Ind AS, a government grant can either be in the nature of –

1. Asset related grant; or
2. Income related grant.

The concept of grant in the nature of promoter's contribution has been done away with.

a Accounting for capital grants - Though there is no significant difference between recognition and measurement of asset related grants under both the GAAPs, presentation of grants in books of accounts is vastly different. Previous GAAP allowed asset related grant, either to be deducted from the cost of the asset on initial recognition or to be recognised as deferred income and recognised over the useful life of the assets.

Under Ind AS, grants irrespective of the underlying purpose, are always recognised as deferred income and amortised in income statement in the period over which benefits are availed. This will have impact on both the sides of profit & loss. The income side will have grant income getting credit over useful life of the assets and the expenses side will be impacted by additional depreciation for the fixed assets. This adjustment will increase the EBITDA, but will have negative impact on return on capital employed.

Impact upon transition

For capital grants recognised as a reduction from fixed assets – Upon transition to Ind AS, all those grants for which the period has not expired as on the date of transition will be restated in the books, to the extent of unamortised portion with a corresponding adjustment to WDV of the related property, plant and equipment.

For grants categorised as promoter contribution – Since there is no such concept in Ind AS, such grants will be moved out of equity and recognised as deferred income, after amortising the portion of grant for the expired period.

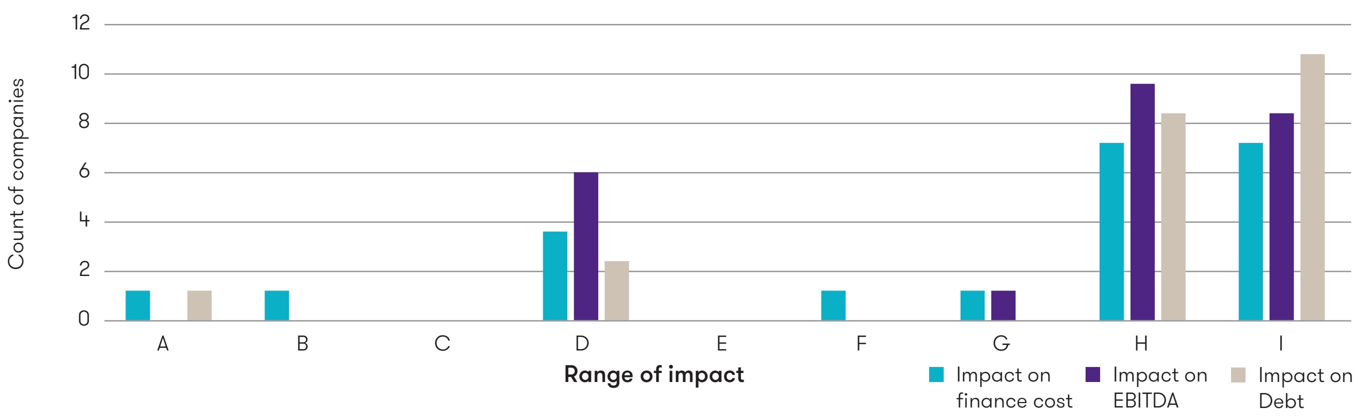
These adjustments have a direct impact on equity of the companies along with the other performance metrics. Out of 37 companies, 3 companies have made this adjustment. Maximum impact reported under this adjustment is Rs 92 crore on equity with average impact of around Rs. 14 crore on the income statement. However, the amortisation of grant on a systematic basis in the statement of profit & loss will have a positive impact on P&L going forward.

b Accounting for grants through off-market loans – Under previous GAAP, there was no specific guidance to account for loan provided by the government at the interest rate below the market rate of interest as well as for forgivable loans.

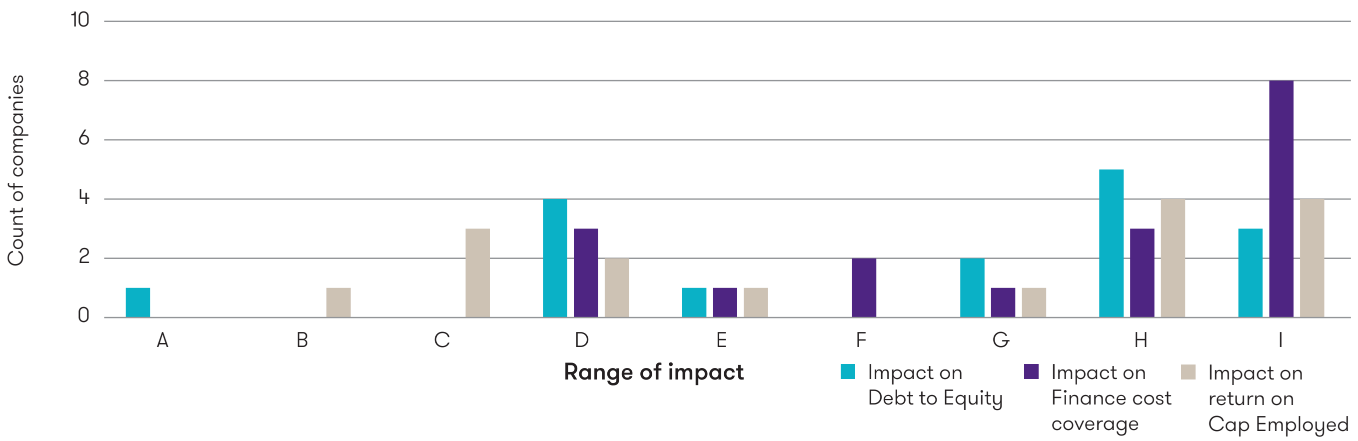
Under Ind AS, in case a loan provided by the government is below the market rate, the difference between the fair value of the loan and the transaction price is required to be accounted for as a government grant. This adjustment will increase the finance costs of the companies on one side and recognition of grant income on the other. This will have positive impact on EBITDA and negative impact on return on capital employed of the companies.

The charts below depict the impact of government grants and other adjustments on certain key performance metrics and ratios, which are largely in the range of +/-5 per cent, with equivalent number of companies being impacted by over -20 per cent:

Impact on key performance metrics



Impact on key performance ratios



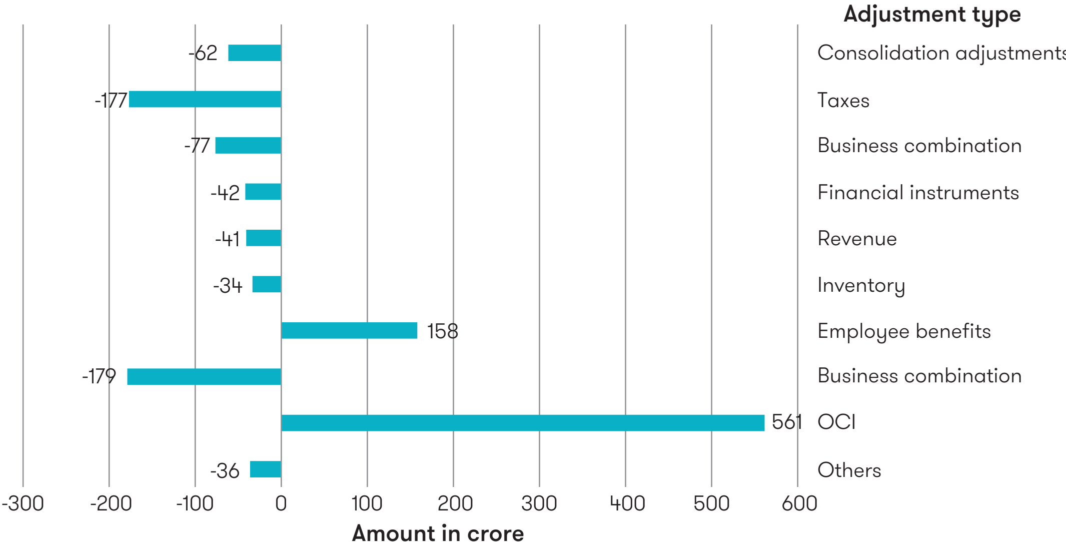
A: 5%-10% **B:** 10%-15% **C:** 15%-20% **D:** > 20% **E:** (5%)-(10%)
F: (10%)-(15%) **G:** (15%)-(20%) **H:** < (20%) **I:** (5%)-5%

Sector-wise analysis: Information Technology (IT)

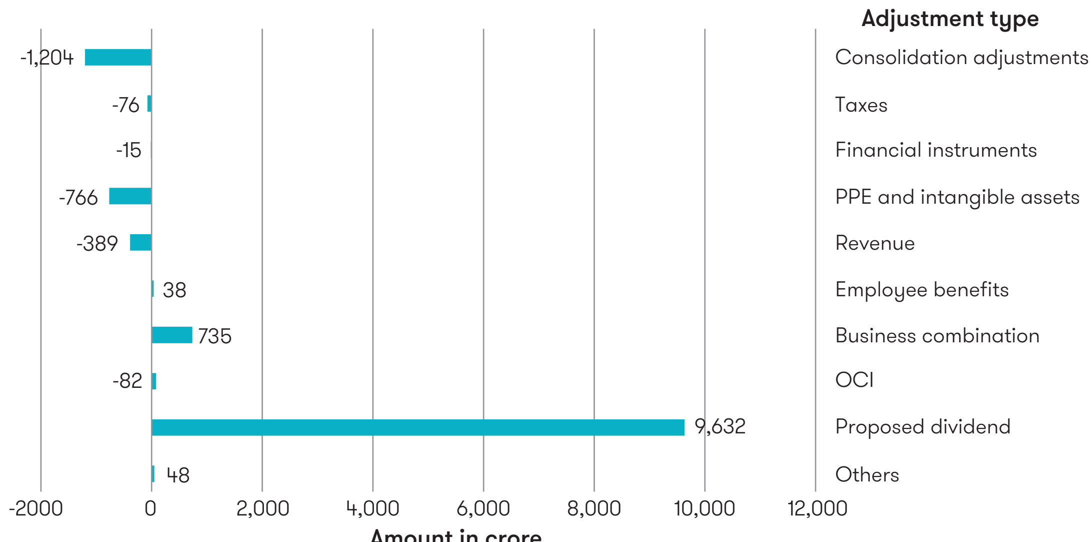
The big picture

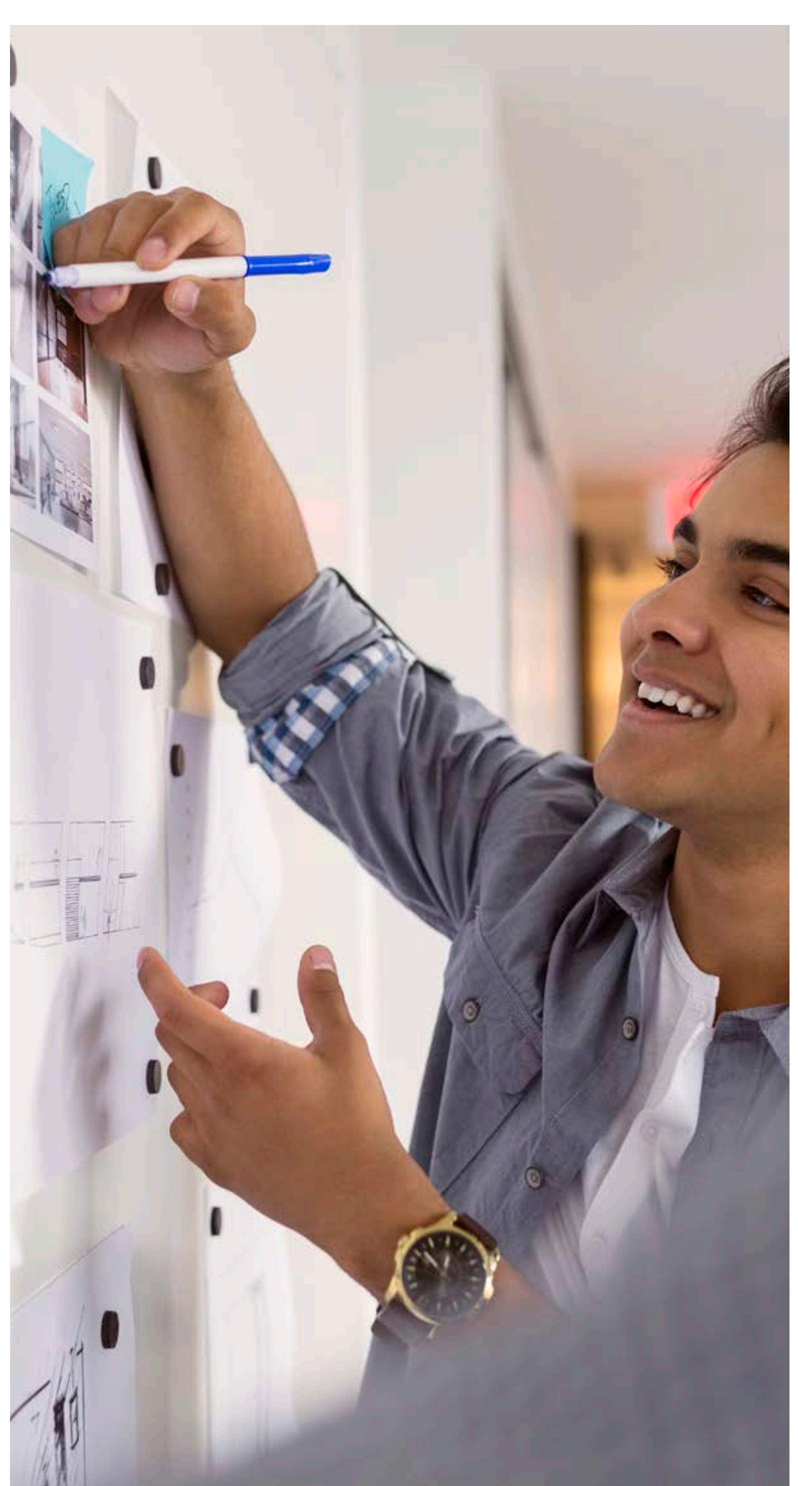
A total of 29 listed companies, with primary business operations in this sector were considered for financial results analysis.

Impact on total comprehensive income for FY ended 31 March 2016 under Ind AS as compared to IGAAP (Rs. crore)



Impact on Equity as at 31 March 2016 under Ind AS as compared to IGAAP (Rs. crore)





In the current era, IT is the lifeline of every business. IT sector has played a significant role in India's growth story. Further, this sector is supported by Indian Government's Digital India Movement. It is one of the favourite sectors for investors although, growing competition may see more consolidation in the near future. In the last few years, IT has made a massive impact on all business houses. The need to know the change in the accounting principles that affect this sector would be certainly one of the top most items on an investor's list considering the huge amount of investments that are already made in this sector.

The key adjustments in this sector that have contributed to the change in net profit and net equity under Ind AS from existing Indian GAAP comprise – revenue recognition, adjustments pertaining to tangible and intangible assets, business combinations and consolidation. Whilst most adjustments have had a mild impact on the financial statements of companies in this sector, however, impact of consolidation assessment resulting in inclusion of new entities, adjustment in share of non-controlling interest, etc. have had significant impact as discussed below.

Consolidation – subsidiaries, associates and joint ventures

The new standard on consolidation under Ind AS brings in a lot of diversity from the previous GAAP as Ind AS 110 is driven by substance based accounting as against rule based consolidation under AS 21.

Under Indian GAAP, control was defined as:

a Ownership, directly or indirectly through subsidiary(ies), of more than one-half of the voting power of an entity; or
b Control of the composition of the board of directors or corresponding governing body so as to obtain economic benefits from its activities.

However, the corporate renaissance that has largely contributed to the growth story for most of the corporates goes beyond the realm of plain vanilla contracts that grant control through the aforementioned channels. More often than not, larger exposure to risks and returns through more complex arrangements has been witnessed. It is not surprising, thus, that many companies have been able to keep certain undesirable structures out of their consolidated financial reporting by complying with water-tight definition above. Further, interestingly, following the above definition, an entity can be subsidiary of two entities when, as per the definition of the term 'control', the entity is controlled by both the entities — one through control over the governing body and the other through majority in voting power.

The new accounting rules adopt a principles-based approach to the definition of 'control' and prescribe consolidation in many such circumstances, which, under the existing standards, would not have warranted consolidation. Under the new definition of 'control', an investor **controls** an investee if and only if the **investor has all the following**:

a **power** over the investee, giving the investor existing rights to direct the relevant activities that affect its returns;
b **exposure**, or rights, **to variable returns** from its involvement with the investee; and
c **ability** to use its power over the investee to affect the amount of the investor's returns.

Ind AS 110 also unfolds guidance in circumstances where power of shareholders with majority voting interest may be restricted in certain aspects by approval or substantive veto rights granted to minority shareholders or providers of sub-ordinate debt. Sometimes these rights may have little or no impact on the ability of majority shareholders or alternatively those rights may be so restrictive to call into question whether control rests with the majority owner. Who ultimately controls is a subject of thoughtful evaluation based on facts and circumstances in every case.

Some of the typical aspects of consolidation guidance relevant for assessment of control in comparison to previous GAAP have been detailed below:

a **De-facto control** – As per Ind-AS 110, an investor might have a control over an investee even if he/she does not have more than majority of the voting rights of that investee. De-facto control exists if the investor has the practical ability to direct the relevant activities of the investee. This depends upon the size of the investor's holding vis-à-vis the holding by others, potential voting rights or any form of contractual arrangements. This concept was not there under previous GAAP.
b **Potential voting rights** – Under previous GAAP, convertible instruments were not considered while determining voting rights of the investee. Ind AS 110 requires the investor to assess control after considering the voting rights achieved from convertible instruments which gives it the power to direct the relevant activities of the investee another entity.

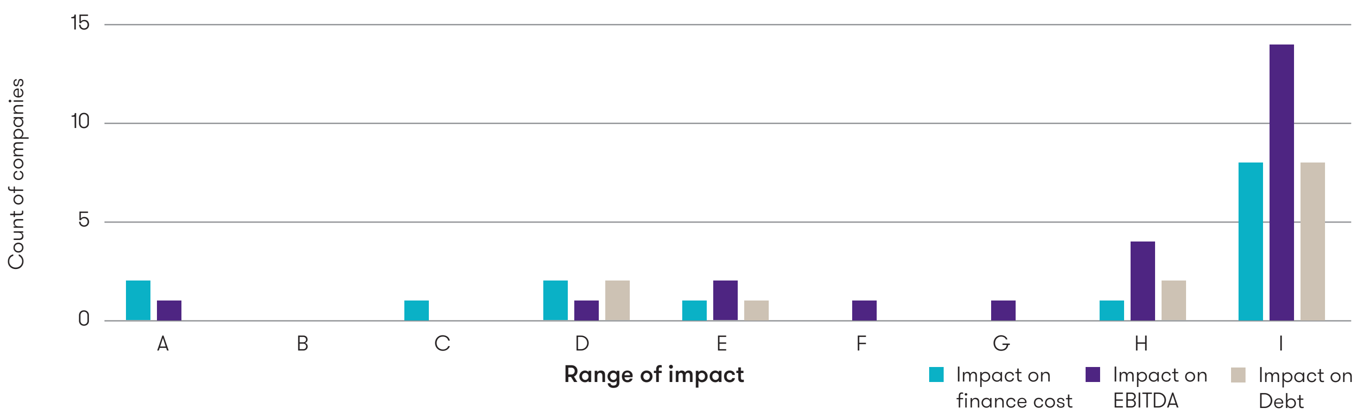
The new standard will have double fold impact on the Indian Companies. On one hand, it brings more entities within its ambit like special purpose vehicles, trust, partnership firms, etc., but on the other hand, it may lead to deconsolidation of some of the entities consolidated earlier because of de-facto control, potential voting rights, no control over relevant activities or principal agent considerations. Business houses, have to update their existing group structures and start coordinating with new group entities to achieve compliance with Ind AS 110.

Impact upon transition

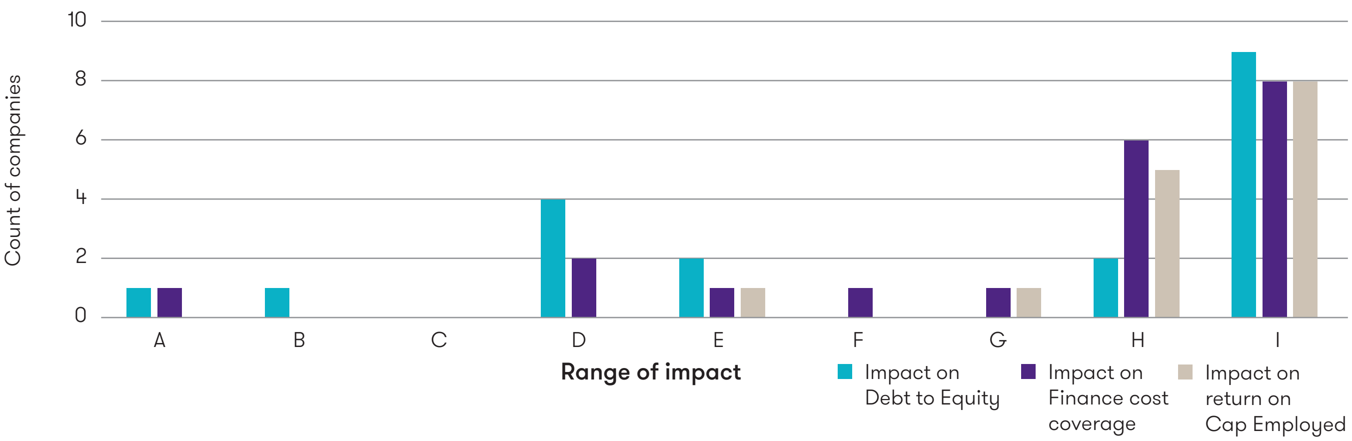
Assessment of entities to ascertain control under Ind AS 110 may significantly impact the asset and liability size of the consolidated financial statements. On account of these adjustments, there is a negative impact on the sector – approximately Rs. 1,204 crore on equity reported as of 31 March 2016. This is clearly indicative of loss making entities that were outside the ambit of group under existing Indian GAAP, but which now will continue to reflect in the results of the holding company reporting under Ind AS.

The charts below depict the impact of above adjustment along with certain others on the key performance metrics and ratios for the sector:

Impact on key performance metrics



Impact on key performance ratios



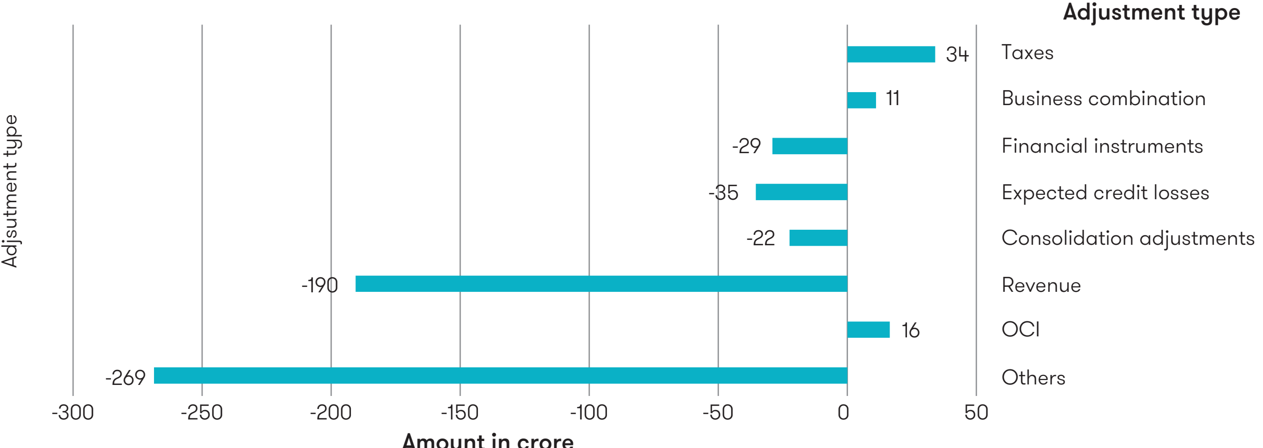
A: 5%-10% **B:** 10%-15% **C:** 15%-20% **D:** > 20% **E:** (5%)-(10%)
F: (10%)-(15%) **G:** (15%)-(20%) **H:** < (20%) **I:** (5%)-5%

Sector-wise analysis: Media and entertainment

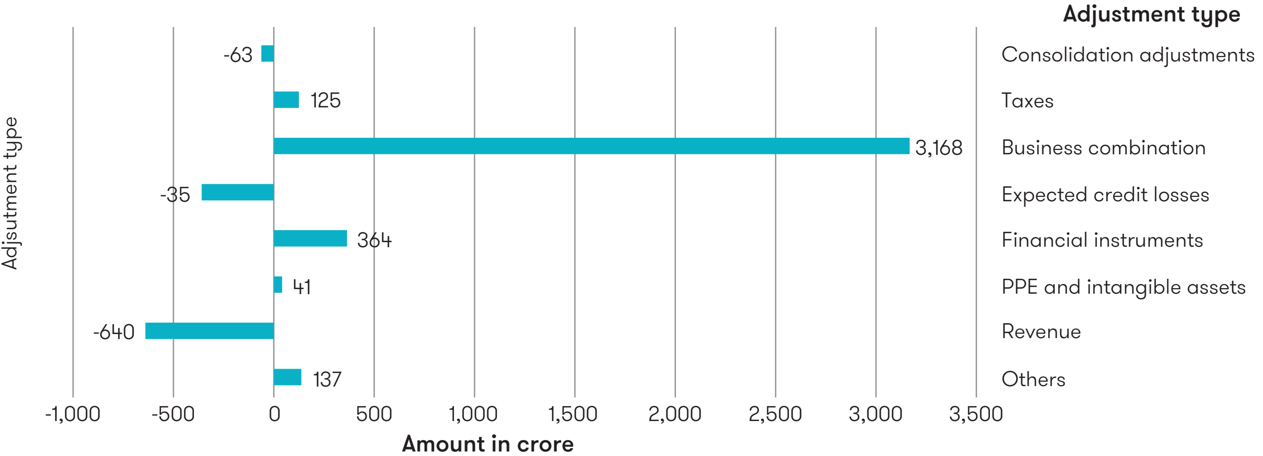
The big picture

A total of 24 listed companies, with primary business operations in this sector were considered for financial results analysis.

Impact on total comprehensive income for FY ended 31 March 2016 under Ind AS as compared to IGAAP (Rs. crore)



Impact on Equity as at 31 March 2016 under Ind AS as compared to IGAAP (Rs. crore)



The Indian media and entertainment (M&E) industry is a sunrise sector for the economy and is making high growth strides. Proving its resilience to the world, the Indian M&E industry is on the cusp of a strong phase of growth, backed by rising consumer demand and improving advertising revenues. The industry has been largely driven by increasing digitisation and higher internet usage over the last decade. Internet has almost become a mainstream media for entertainment for most of the people.

The advent of Ind AS impacted this industry on several fronts with the key adjustments being – business combinations, fair value measurement for revenue and financial instruments. Amongst these, accounting for business combinations has had a significant impact on this sector, which has been analysed in greater detail below:

Business combinations

Ind AS contain comprehensive guidance on identification, measurement and disclosure of business combination transactions. Some of the key areas to be watchful about are discussed below:

a **Increased role of fair valuation exercise:**
- On acquisition of a business, all identifiable assets and liabilities are recorded at their respective acquisition date fair values. A key point to note here is that identifiable assets also include intangible assets that were not recognised by the acquired entity e.g. customer contracts/ relationships, technology platform, brands, non-compete agreements, etc.
- In addition, non-controlling (or minority) interests (NCI) can also be measured at their acquisition date fair values.
- Purchase consideration other than cash e.g. shares, bonds, etc., are recognised at their fair value.

This is a significant shift from the existing accounting guidance which mainly requires use of book values.

b **Scope of purchase consideration:**
While the existing literature specifies the scope of purchase consideration to include securities, cash or other assets; the new standard provides detailed guidance which states that purchase consideration includes payments in cash, shares, bonds, assets, etc. that are made
- at the time of the transaction,
- or at a later date (deferred consideration)
- or based on contingent events (contingent consideration) e.g. minimum average return on investment over a period, as long as these payments relate to the transaction. Deferred consideration is recorded at present value and contingent consideration is recorded at its fair value, with subsequent movements in these values being recognised in the income statement.

c **Accounting for difference between purchase consideration and fair value of net assets/liabilities acquired:**
Conceptually, nothing much has changed here. The excess of purchase consideration plus NCI over the fair value of net assets is recognised as goodwill. If the same is negative, it is recognised in Other Comprehensive Income ('OCI') and accumulated as capital reserve in equity. However, unlike the existing literature which doesn't prohibit amortisation of goodwill, the new rules require only an annual testing of goodwill for impairment and amortisation is prohibited.

d **Fair valuation of pre-existing relationships:**
In a business combination, where the acquirer had some pre-existing relationship with the acquired entity, the acquirer's accounting for such relationships may differ depending on whether settlement of such transactions are part of the business combination or are separate transactions. Accounting for transactions that exist or are entered into at the time of business combinations, but are distinct from the business combination transactions, are accounted in accordance with the relevant Ind AS.

e **Deferred taxes:**
All temporary differences arising as a result of the business combination give rise to deferred taxes. For example, an asset recognised at fair value on account of a business combination might still be measured at cost for income tax purposes. No deferred tax is recognised on goodwill.

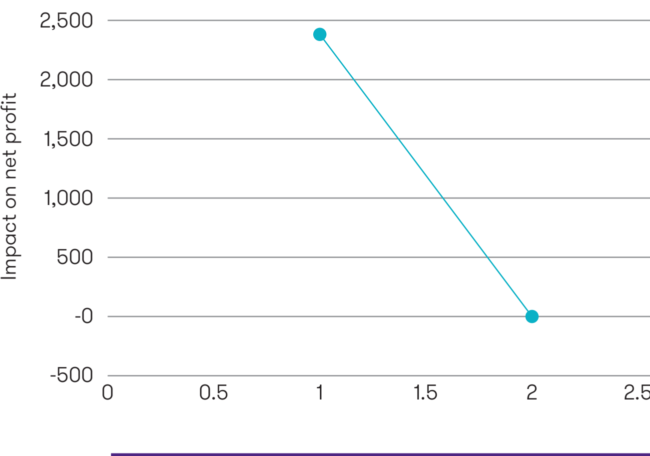
> **Impact upon transition**
> Accounting for business combinations kicks in for acquisition of corporate legal as well as for purchase of group of assets (net of liabilities) which comprise a business. For instance, if the acquisition of business is through slump sale arrangement, then the same is accounted in standalone financial statements applying Ind AS 103.

Accounting for assets and liabilities in a business combination has a clear impact on the financial performance:

1. Change in key metrics like – depreciation, finance cost, EBITDA, etc. in both standalone and consolidated financial statements.
2. Impact on key ratios – Further, the recognition of assets and liabilities at fair value has a direct impact on the key ratios like debt coverage, return on capital employed, etc. which in turn may also affect the loan covenants for a lot of companies.

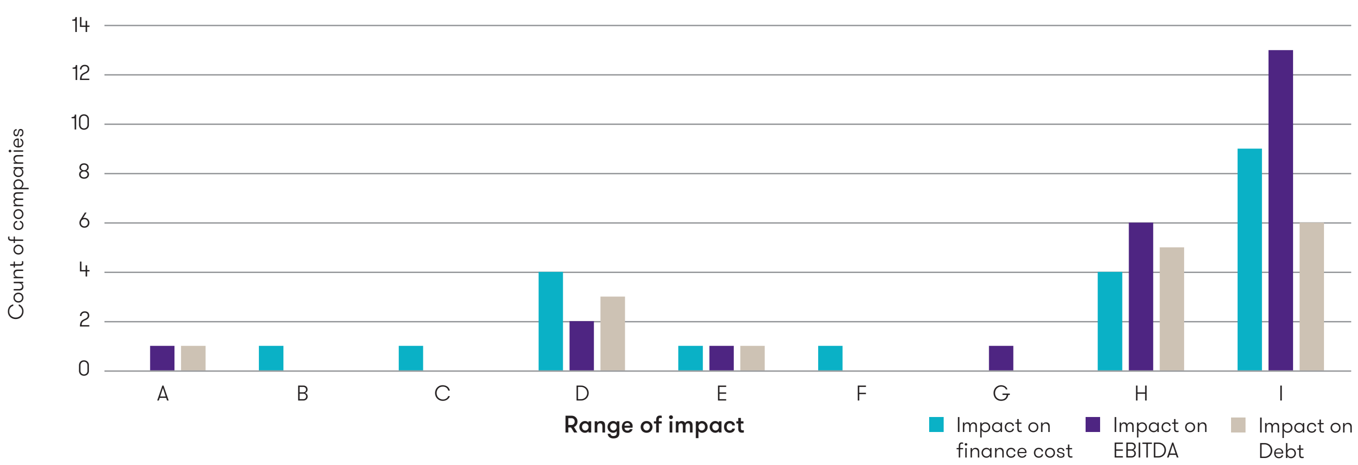
The total adjustments reported in this sector on account of above indicate an impact of Rs. 3,168 crore on equity and Rs. 11 crore on net profit. However, the maximum impact being INR 2,355 crore and minimum (negative) impact of Rs. 5 crore on equity as of 31 March 2016 has been reported by companies under Ind AS.

Maximum and minimum impact

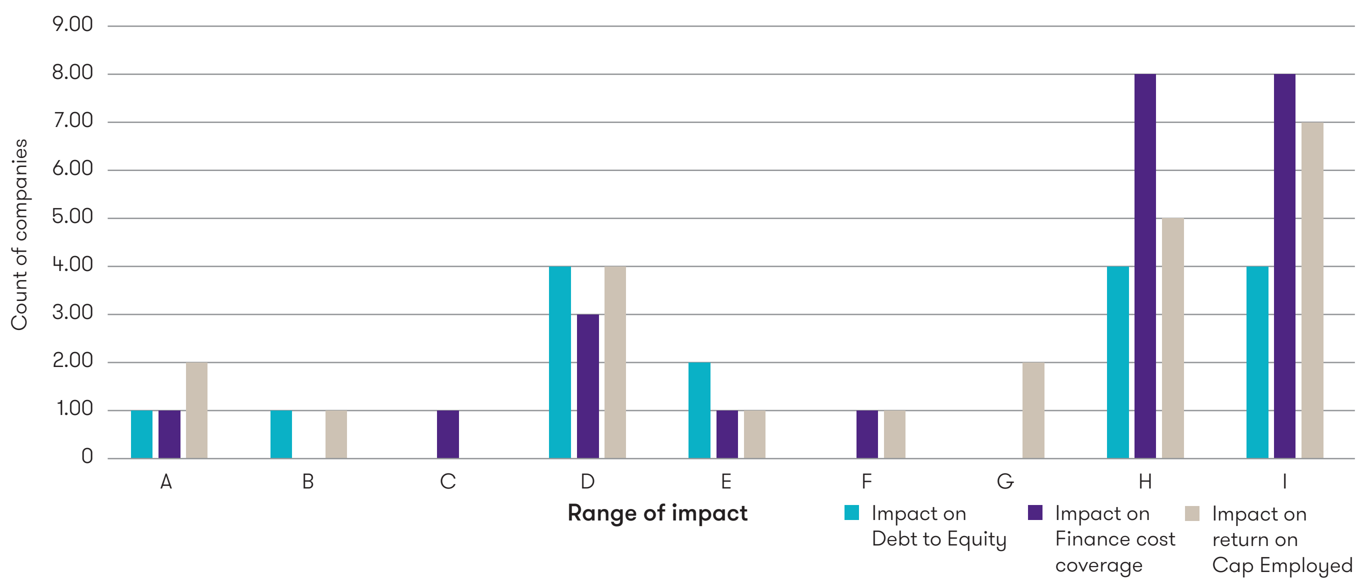


The charts below depict the impact on the key performance metrics and key performance ratios for the sector:

Impact on key performance metrics



Impact on key performance ratios



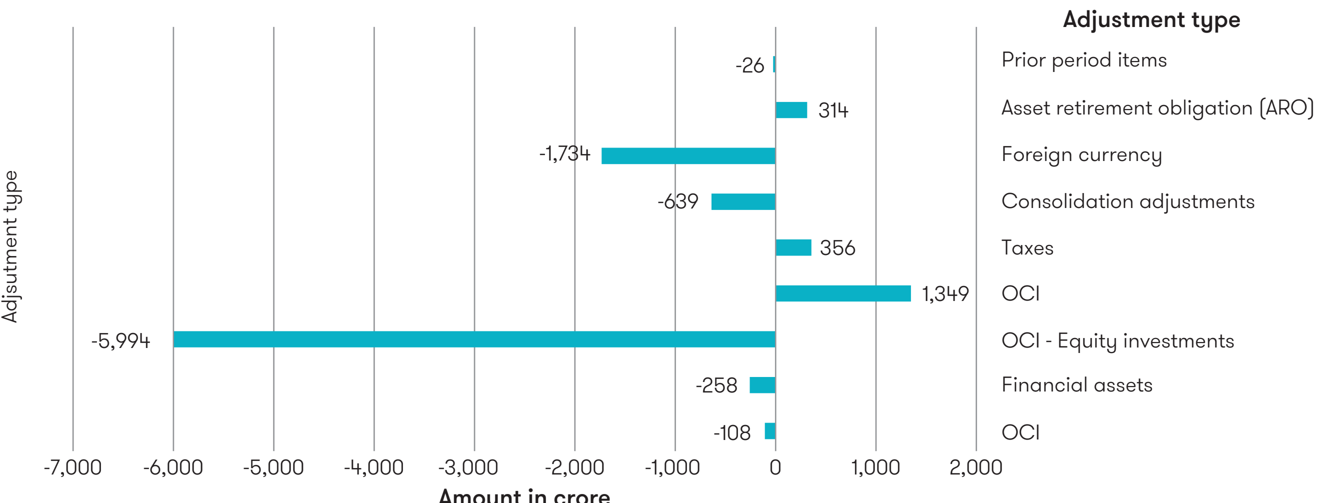
A: 5%-10% **B:** 10%-15% **C:** 15%-20% **D:** > 20% **E:** (5%)-(10%)
F: (10%)-(15%) **G:** (15%)-(20%) **H:** < (20%) **I:** (5%)-5%

Sector-wise analysis: Oil Gas and Mining

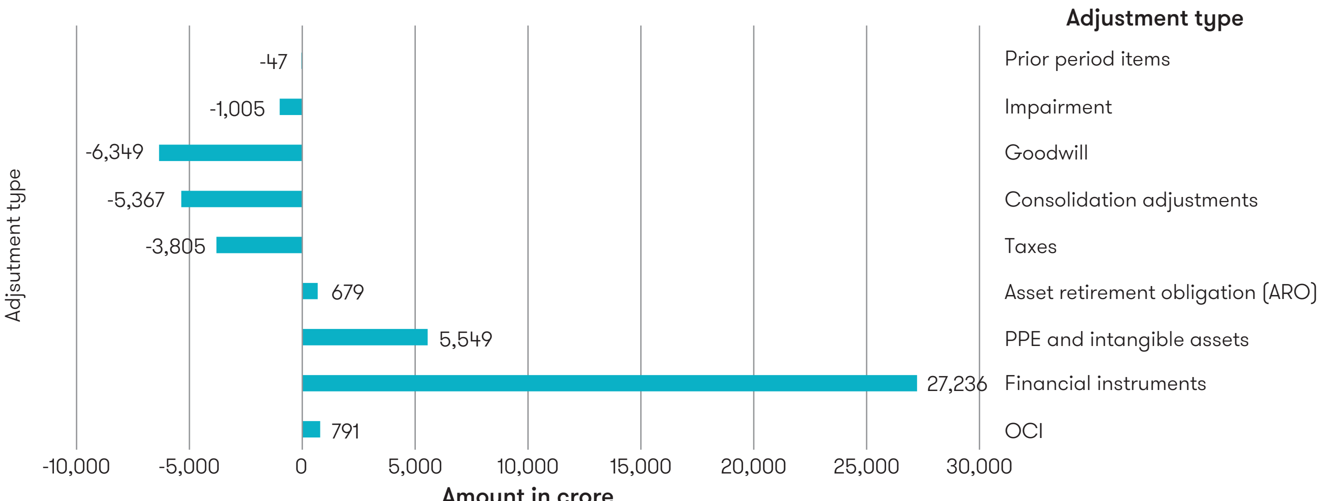
The big picture

A total of 25 listed companies, with primary business operations in this sector were considered for financial results analysis.

Impact on total comprehensive income for FY ended 31 March 2016 under Ind AS as compared to IGAAP (Rs. crore)



Impact on Equity as at 31 March 2016 under Ind AS as compared to IGAAP (Rs. crore)



The oil, gas and mining sector is among the core industries in India and plays a major role in influencing decision making for all the other important sections of the economy. Oil and Gas sector is one of the 25 key areas under 'Make in India' initiative. India was the third largest consumer of oil in the world in 2015, after the United States and China. This sector is expected to experience significant growth in the coming years. With expenditures like, exploration and evaluation, mine development, mine closure expenditure, stripping cost etc. this sector is set to experience key accounting changes with Ind AS.

This sector has been a witness to some significant impacts upon convergence to Ind AS, with key adjustments being – accounting for financial instruments, adjustments in property, plant and equipment and fair valuation of investments through other comprehensive income (FVOCI). Since this sector has seen huge FVOCI adjustments, the same have been analysed below.

Fair value through other comprehensive income

Ind AS mandates the use of fair value for all investments in equity instruments (expect those in subsidiaries, joint ventures and associates). An investment in portfolio of shares that is held for making short term profit based on market movements is classified as Fair value through Profit and loss ('FVTPL'), since the objective is to realise the marked to market movement.

On the other hand, if a company makes strategic investment in equity shares of another entity, such investments can either be classified as fair value through OCI (FVTOCI) or FVTPL. The investments in FVOCI category are required to be carried at fair value, with fair value gains/losses recognised in OCI and not reclassified to P&L.

The option chosen will have a significant impact on EBITDA and net profit, and FVOCI option removes all volatility from the P&L. It was observed to be the chosen option by the industry constituents.

Impact upon transition

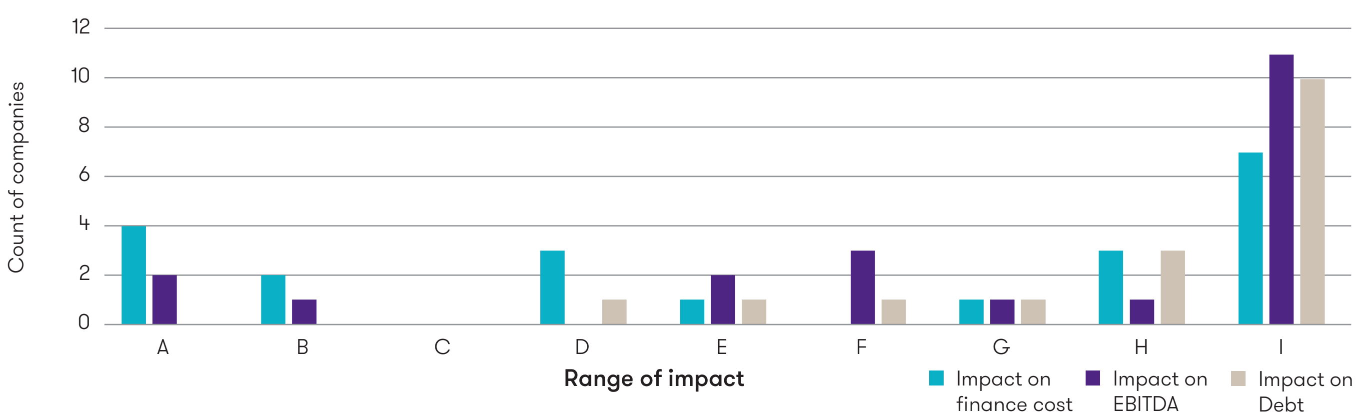
Around seven companies in the industry were observed to have a cumulative positive impact of Rs. 313.68 crore on net profit for the year ended 31 March 2016 and cumulative positive impact of Rs. 26,134.68 crore on total equity as at 31 March 2016. With respect to treatment for Minimum Alternate Tax provisions of the Income Tax Act, it was clarified that the Gains and losses from investments in equity instruments designated at FVOCI shall be included in book profits at the time of realisation.

Certain companies had to carry their investments in debt instruments at fair value through profit and loss. This is in contrast with Indian GAAP where long term investments are carried at cost, and current investments are carried at lower of cost and fair value.

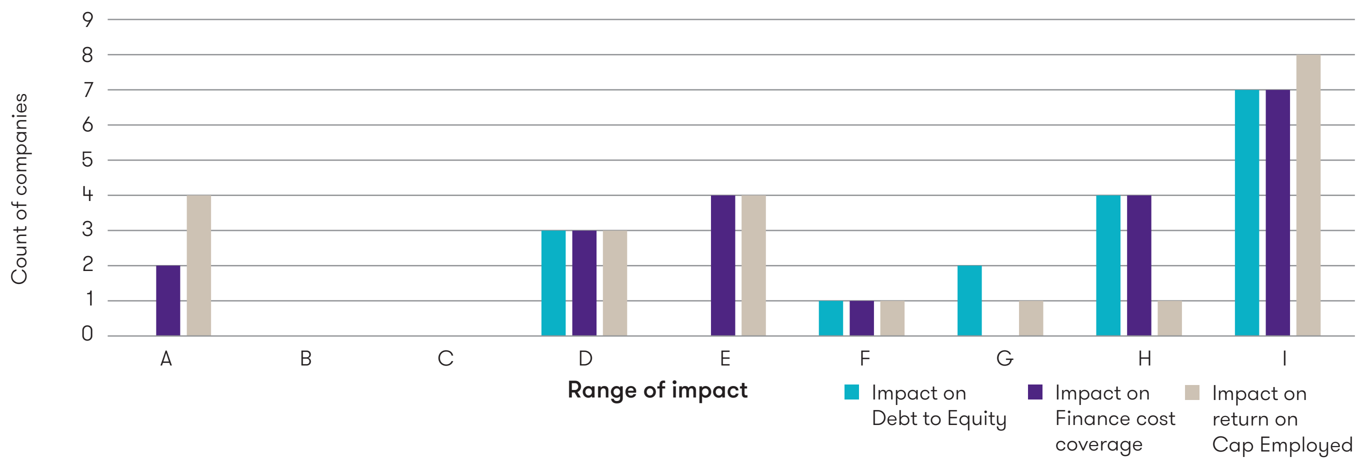
Clearly, Ind AS provides an opportunity to classify financial assets/ liabilities under categories whose measurement basis corresponds to the purpose of asset and its realisability.

The charts below depict the impact on the key performance metrics and key performance ratios for the sector:

Impact on key performance metrics



Impact on key performance ratios



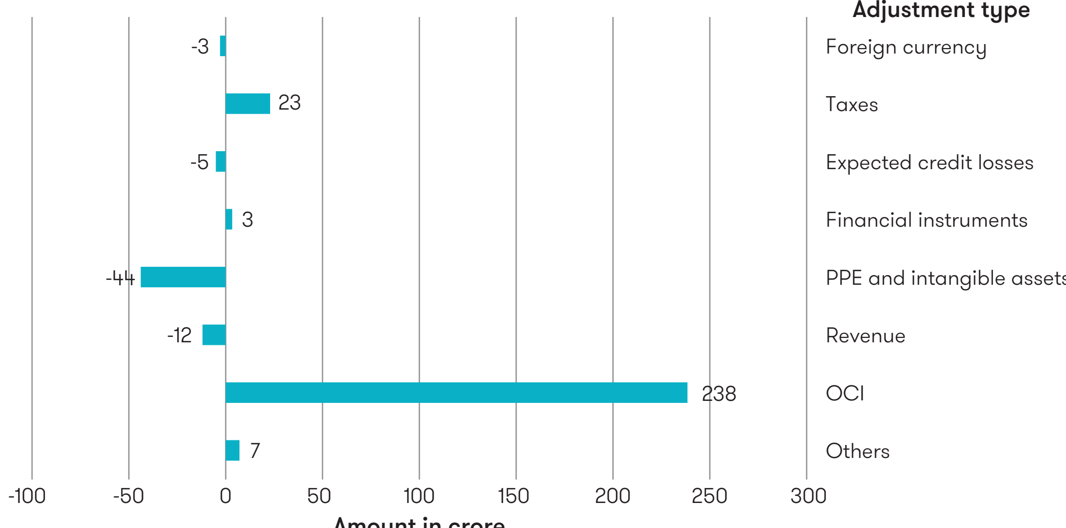
A: 5%-10% **B:** 10%-15% **C:** 15%-20% **D:** > 20% **E:** (5%)-(10%)
F: (10%)-(15%) **G:** (15%)-(20%) **H:** < (20%) **I:** (5%)-5%

Sector-wise analysis: Retail

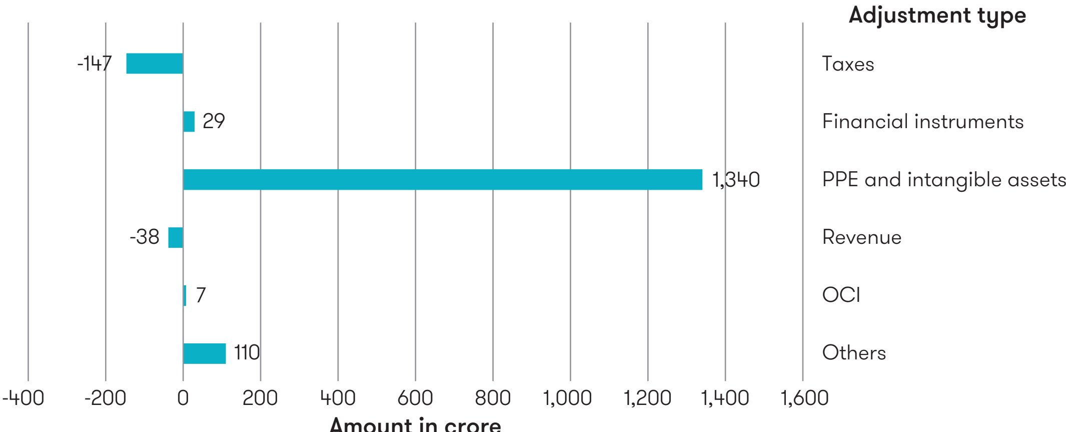
The big picture

A total of nine listed companies, with primary business operations in this sector reported under Ind AS. The impacts on net profit and equity have been summarised below:

Impact on total comprehensive income for FY ended 31 March 2016 under Ind AS as compared to IGAAP (Rs. crore)



Impact on Equity as at 31 March 2016 under Ind AS as compared to IGAAP (Rs. crore)



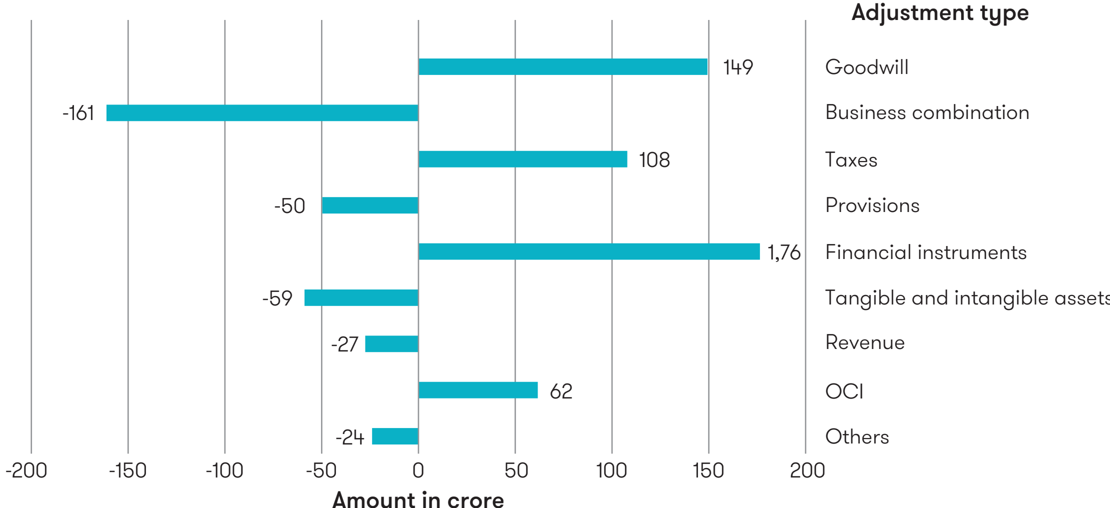
Basis the analysis of the results of companies in this sector, the adjustments largely pertained to fixed assets (for change in depreciation, adjustment of forex losses, etc.) and impacts recognised in OCI. Other than these, no significant individual adjustments seemed to be made.

Sector-wise analysis: Pharma

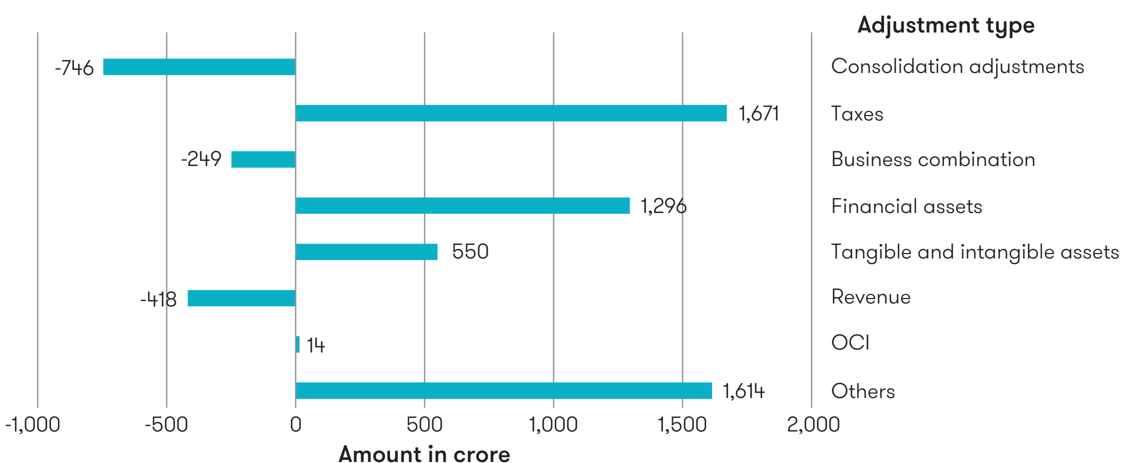
The big picture

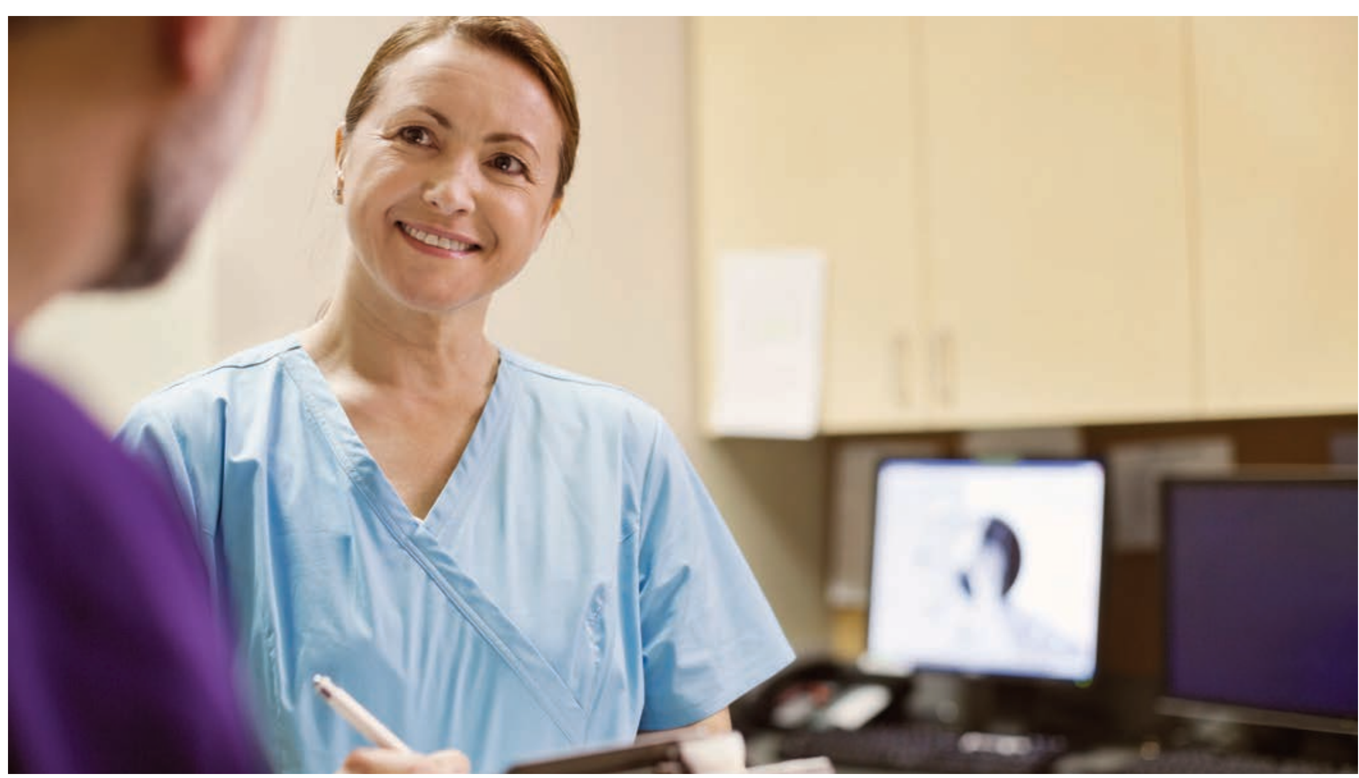
A total of 29 listed companies, with primary business operations in this sector were considered for financial results analysis.

Impact on total comprehensive income for FY ended 31 March 2016 under Ind AS as compared to IGAAP (Rs. crore)



Impact on Equity as at 31 March 2016 under Ind AS as compared to IGAAP (Rs. crore)





The Indian pharmaceuticals market is the third largest in terms of volume and thirteenth largest in terms of value. India is the largest provider of generic drugs globally with the Indian generics accounting for 20 per cent of global exports in terms of volume. The sector comprises a range of sub sectors such as pharmaceuticals, biotechnology, medical equipment, etc. facing a common set of Ind AS issues, such as measurement of financial instruments, capitalisation of stores and spares which can be used for more than one period, fair valuation of stock options, recording provisions using expected credit loss model etc.

Amongst the Ind AS adjustments impacting this sector, accounting for cash flow hedges was seen to be adopted by several companies, which has been analysed in detail below:

Cash flow hedge

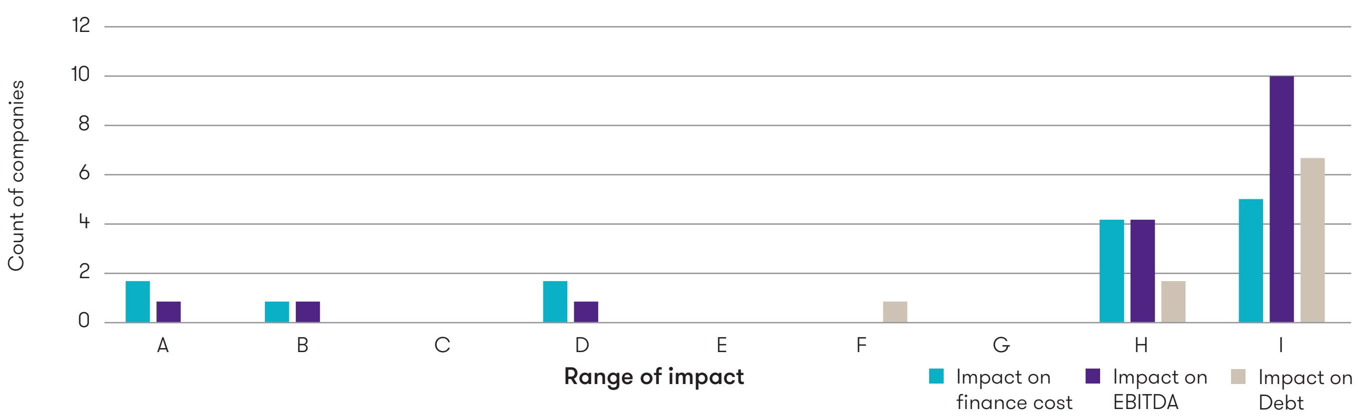
With introduction of Ind AS in India, certain items of expense and income are required to be routed through other comprehensive income ('OCI'), such as, re-measurement gain/(loss) on defined benefit obligation, fair value changes in equity investments, fair value changes in debt investments carried at FVOCI, foreign exchange translation of foreign operations. The above adjustment constitutes an impact of Rs 213 crore to profit and Rs81 crore on equity. Maximum impact being Rs162.12 crore and minimum (negative) impact of Rs 4.97 crore.

Further, under the previous GAAP, the underlying foreign currency instrument is recognised at transaction cost and related derivative is either not accounted for or loss is booked basis mark to market statement. Whereas, Ind AS gives an option to carry out hedge accounting i.e. fair value hedge and cash flow hedge.

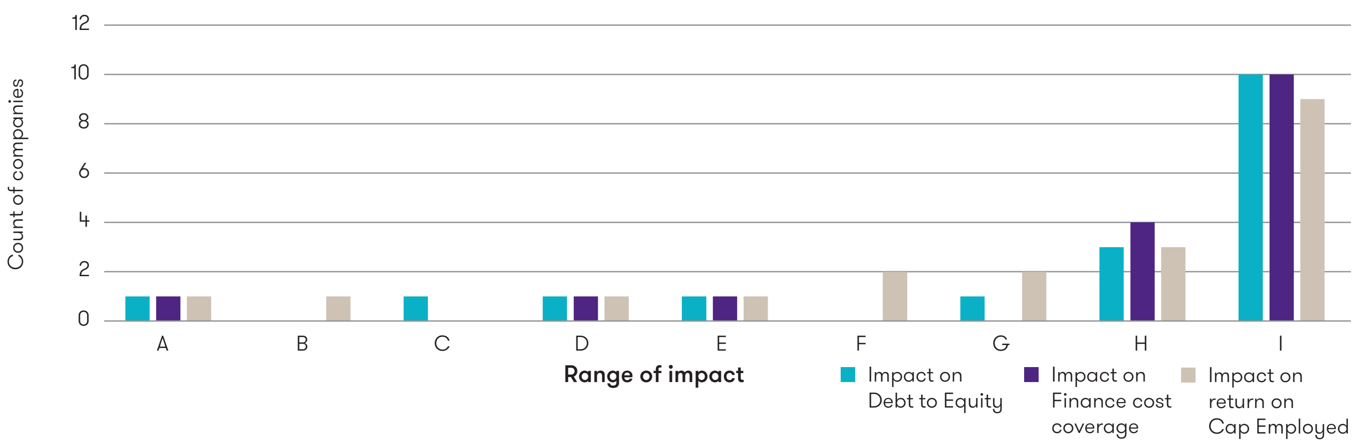
Under cash flow hedge, the gain or loss related to the hedged item is neutralised through a transfer of an amount from the other comprehensive income, recognised in respect of the fair value changes related to the hedging instrument. Only the ineffective portion of the change in fair value of hedging instrument is recognised in income statement until settlement. Upon settlement, the carrying amount in cash flow hedge reserve is reclassified to profit & loss. The entities may choose this option to avoid volatility in their statement of profit and loss.

The charts below depict the impact of above adjustment along with certain others on the key performance metrics and key performance ratios for the sector:

Impact on key performance metrics



Impact on key performance ratios



A: 5%-10% **B:** 10%-15% **C:** 15%-20% **D:** > 20% **E:** (5%)-(10%)
F: (10%)-(15%) **G:** (15%)-(20%) **H:** < (20%) **I:** (5%)-5%

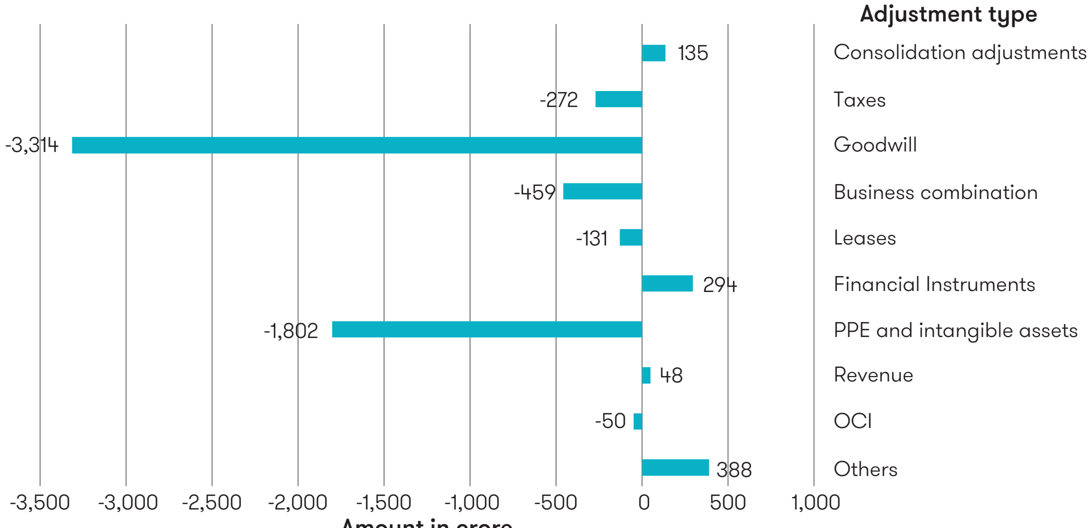
Sector-wise analysis: Logistics

The big picture

A total of 17 listed companies, with primary business operations in this sector were considered for financial results analysis.

Impact on total comprehensive income for FY ended 31 March 2016 under Ind AS as compared to IGAAP (Rs. crore)

Impact on Equity as at 31 March 2016 under Ind AS as compared to IGAAP (Rs. crore)



In recent years, the logistic business is booming because of the economic growth in emerging economies like India, China, etc. leading to an increase in trade between India, China and the rest of the world. With the "just-in-time" ("JIT") management concept developed in recent years, manufacturers, distributors and retailers rely on frequent shipments to sustain production flows and inventory rather than accumulating inventory in their warehouses. This is also accelerating the development of the logistics service business.

The key impact in this industry upon application of Ind AS has been seen in revenue recognition, which has been analysed below.

Revenue

Under the existing Indian GAAP, revenue in case of sale of goods is recognised on transfer of significant risks and rewards of ownership to the customer. In case of most long term contracts, percentage of completion method is used for recognising revenue.

Service contracts
Revenue from service contracts are determined by ascertaining the stage of completion. Under stage of completion method, contract costs, revenue and the resulting profit are recognised in the period in which the work is performed.

No specific method is mandated for assessing the stage of completion. An entity may use the more appropriate method of input measures (consideration of efforts devoted to a contract) or output measures (consideration of the results achieved). The following are methods that can be used to determine the stage of completion, depending on the nature of the contract:

- Surveys of work performed (output measure);
- completion of a physical proportion of the contract work (output measure); or
- percentage of contract costs incurred in relation to total estimated contract costs (input measure).

Agency relationship:
In an agency relationship, amounts collected on behalf of and passed on to the principal are not revenue of the agent. Determining whether an entity is acting as an agent or principal is based on an evaluation of the risks and responsibilities taken by the entity, involving inventory risk and responsibility for the delivery of goods or services. Usually, an entity working as an agent or broker does not have exposure to the significant risks and rewards of ownership of goods or rendering of services. An entity having exposure to the significant risks and rewards associated with the sale of goods or rendering of services is acting as a principal.

Indicators that an entity is acting as a principal include that it:

- -Has primary responsibilities for providing the goods and services to the customer or for fulfilling the order;
- Has inventory risk before or after the customer order, during shipping or on return;
- Has discretion in establishing prices (directly or indirectly);
- Bears the customer's credit risk for the amount receivable from the customer.

An indicator that an entity is acting as an agent is that it performs services for compensation on a commission or fee basis, which is fixed in terms of either an amount of currency or a percentage of value of the underlying goods or services provided by the principal.

In logistics industry, most of the Companies operate as an agent as they perform the services for compensation which is generally fixed for a specific destination and is also based on the quantum.

Revenue from transactions, where the entity is acting in capacity of a principal is recognised on a gross basis. Where the entity is acting as an agent, revenue is recognised on a net basis, that is, the entity recognises only the margin on the transaction as income and not the full amount of sale and cost. Some of the factors that are considered in determining if the entity is acting as a principal are as below:

- the entity has the primary responsibility for delivering the goods or services for the transaction;
- the entity bears the inventory risk;
- the entity has latitude in establishing prices;
- and the entity bears the credit risk for the amount receivable from the customer.

To determine whether revenue should be presented gross or net of costs incurred, the entity considers whether it is acting in the capacity of an agent or principal.

Impact upon transition
There is an overall decline of INR 1100 crore primarily on account of establishment of agency relationship resulting in de-recognition of revenue on net basis (,ie, only commission in comparison to gross sales under previous GAAP) and a corresponding impact reduction of expenses. While overall profit is not affected, revenue declined by 35 per cent.

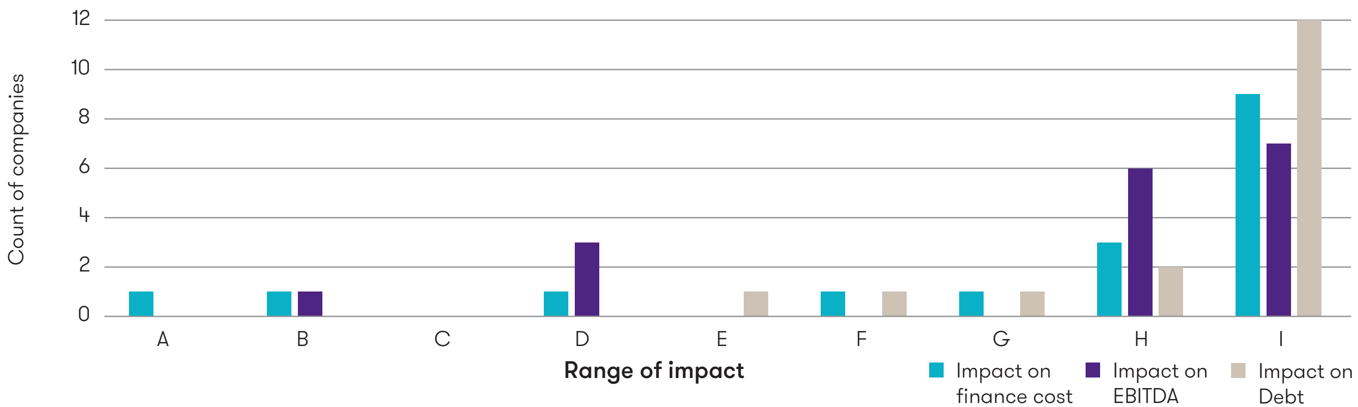
On an overall basis there is an increase in net profit as reported under Ind AS by 41 per cent i.e. INR 610 crore as compared to previous GAAP.

The charts below depict the impact on key performance ratios and metrics:

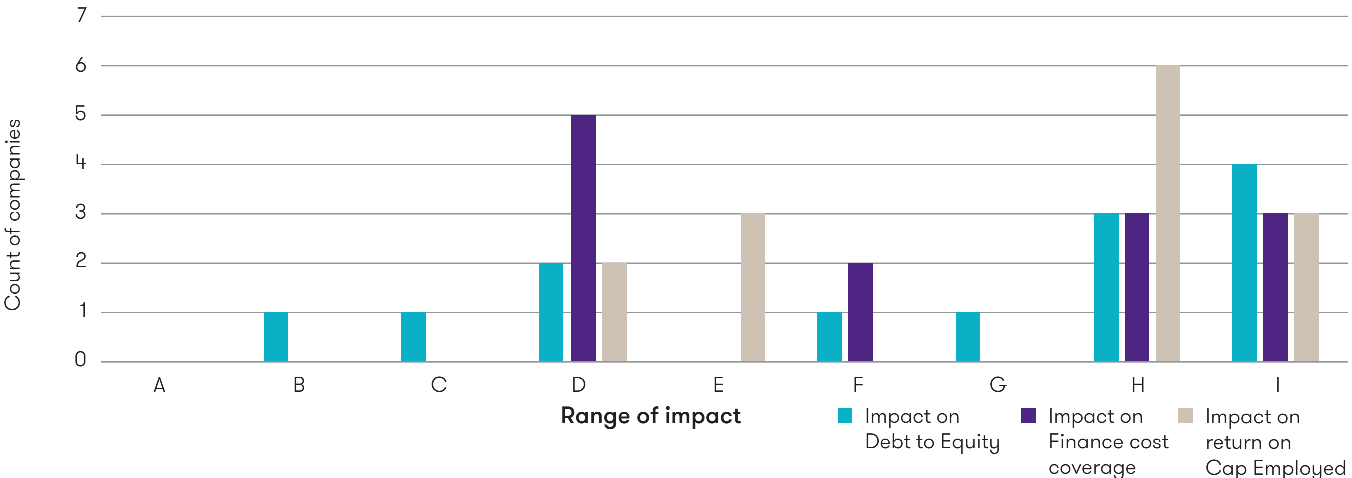
On account of application of Ind AS, the average change in debt to equity ratio is 26 per cent with the maximum positive impact of 468 per cent and maximum negative impact of 91 per cent. Further, finance cost has declined at an average of 14% with 3 companies reported decrease in finance cost by more than 20 per cent with the maximum impact on account of decrease in finance cost is 100 per cent and one company has reported increase in finance cost by 49 per cent.

Also, return on capital employed has declined by an average of 42 per cent. 14 companies have an impact on return on capital employed out of which six companies have negative impact of more than 20 per cent with the maximum negative impact of 293 per cent and two companies have positive impact of more than 20 per cent with the maximum positive impact of 97 per cent.

Impact on key performance metrics



Impact on key performance ratios



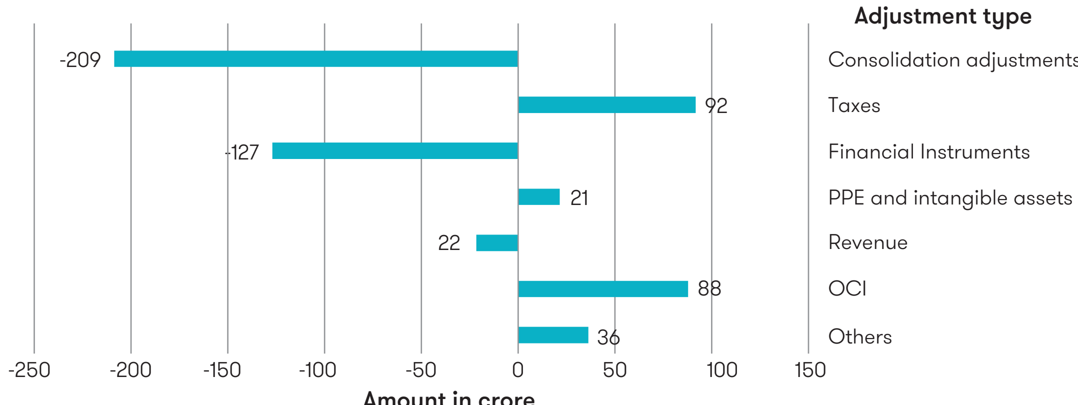
A: 5%-10% **B:** 10%-15% **C:** 15%-20% **D:** > 20% **E:** (5%)-(10%)
F: (10%)-(15%) **G:** (15%)-(20%) **H:** < (20%) **I:** (5%)-5%

Sector-wise analysis: Service

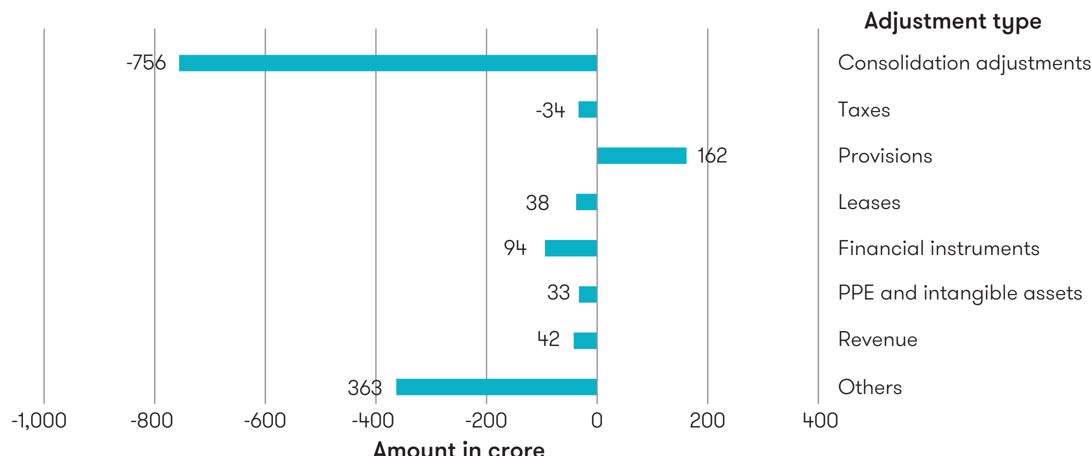
The big picture

A total of 21 listed companies, with primary business operations in this sector reported under Ind AS. The impacts on net profit and equity have been summarised below:

Impact on total comprehensive income for FY ended 31 March 2016 under Ind AS as compared to IGAAP (Rs. crore)



Impact on Equity as at 31 March 2016 under Ind AS as compared to IGAAP (Rs. crore)



Basis the analysis of the results of companies in this sector, Ind AS adjustments largely pertained to change in consolidation structure (including inclusion of new subsidiaries basis control assessment) and small adjustments in fixed assets, reversal of proposed dividend, etc. Other than these, no significant individual adjustments seemed to be made.

MAT implication for Ind AS adjustments

The Finance Act, 2017 introduced an important amendment to specify the applicability of Section 115JB of the Income-tax Act, 1961 ("MAT provisions") on adjustments made to book profits and equity of a company due to transition to Indian Accounting Standards ("Ind-AS"). These amendments are applicable for financial year 2016-17 and are summarised as under:

- The amended provisions propose that the impact of adjustments made to "other equity" upon transition to Ind-AS shall be adjusted in book profits of the company evenly over a period of five years beginning with the convergence year.
- Convergence year and date (for companies with March year-end):

Phase of Ind-AS implementation	Convergence year	Convergence date
Phase 1 (companies other than banks, NBFCs and insurance companies)	2016-17	1 April 2016
Phase 2 (companies other than banks, NBFCs and insurance companies)	2017-18	1 April 2017
Phase 1 NBFCs and banks	2018-19	1 April 2018
Phase 2 NBFCs	2019-20	1 April 2019
Insurance companies	2020-21	1 April 2020

It should be noted that the concept of "convergence date" under MAT provisions is different from the concept of "transition date" under Ind-AS.

- MAT provisions are attracted on adjustments in any head of equity on convergence date except:
  1. capital reserve, and
  2. securities premium reserve

This indicates that certain adjustments which are mere reclassifications between financial liability and equity (example, off-market interest rate loans from related parties) and entail notional debits/ credits in the profit & loss account in later years could also attract MAT provisions.

For instance, if a subsidiary obtains a loan from its parent at concessional interest rate, the difference between the amount of loan and its fair value is credited to equity as a "contribution". This is a notional credit which is compensated by debits to profit or loss in later years on account of notional finance cost on the loan. It is not clear whether under the proposed amendments, such notional credits to equity on the convergence date could attract MAT liability, similar to "equity component of compound financial instruments". The amended provision suggests that the notional finance cost in the profit & loss account would be permissible as a deduction for computing book profits for MAT purposes.

Another example that could be cited here is of a financial instrument classified as a liability under previous GAAP, but as an equity instrument under Ind-AS (like a compulsorily convertible debenture).

It not clear if the amount credited to equity on account of reclassification would be subjected to MAT provisions.

- Applicability of MAT provisions to specific adjustments:

<table>
<tr><th>Nature of adjustment</th><th>Adjustment to equity on convergence date</th><th>Adjustment after convergence date</th></tr>
<tr><td>All adjustments in other comprehensive income (OCI) that will be reclassified to profit or loss (P&L) – for example, cash flow hedge reserve, changes in fair value of financial assets (other than investments in equity instruments) carried at fair value through OCI, gains and losses arising from translating the financial statements of a foreign operation.</td><td colspan="2">Ignored / excluded for MAT purposes (will be included in book profits in the year of reclassification to P&L)</td></tr>
<tr><td>Only following adjustments in OCI that will not be reclassified to P&L:
• Revaluation surplus in respect of property, plant and equipment ("PP&E") and intangible assets
• Gains or losses from investments in equity instruments designated at fair value through OCI ("FVOCI")</td><td colspan="2">Ignored / excluded for MAT purposes*</td></tr>
<tr><td>Adjustments relating to items of PP&E, intangible assets and investments in subsidiaries, joint ventures and associates recorded at fair value as deemed cost on date of transition to Ind-AS</td><td rowspan="2">Ignored / excluded for MAT purposes*</td><td>Depreciation on account of fair valuation is added back</td></tr>
<tr><td>Adjustments relating to cumulative translation differences of a foreign operation on date of transition to Ind-AS</td><td>N. A.</td></tr>
<tr><td>Adjustments on account of distribution of non-cash assets to shareholders in a demerger**</td><td rowspan="2">MAT evenly in 5 years beginning with the convergence year***</td><td>Ignored / excluded for MAT purposes</td></tr>
<tr><td>All other adjustments (including remeasurements of defined benefit plans recognised in OCI)</td><td>MAT in year of adjustment</td></tr>
</table>

*Book profit of the year in which the asset, investment or foreign operation is disposed off, shall be adjusted, by the amount of adjustments which were earlier ignored / excluded from book profits for the purpose of applicability of MAT provisions. Further, depreciation on account of revaluation is added back to book profits.

** The Act has clarified the treatment in case of non-cash assets distributed to shareholders on 'demerger' and adjustment to book values of assets/ liabilities recorded in 'resulting company'. Other cases involving non-cash asset distribution to shareholders viz. other forms of spin-off/ restructuring and recording of assets/ liabilities by transferee companies in such cases should arguably be accorded the same treatment but such scenarios currently remain unaddressed.

*** Based on the Act, the treatment on account of distribution of non-cash assets to shareholders upon demerger appears to be different as on the convergence date vis-à-vis post convergence date. While this may not be in consonance with the overall intent, the Bill proposals are so drafted.

It may be noted that deferred tax relating to aforementioned adjustments is to be ignored.

- For simplification, illustrative formats for MAT computation are given below:

Particulars	Amount
Book profits (before OCI) as per Ind-AS financial statements	XXX
Add / less: adjustment to "other equity" on convergence date on account of revaluation surplus of classes of PP&E and intangible assets and gains or losses from investments in equity instruments designated at FVOCI, sold during the year	XXX
Add / less: adjustment to "other equity" on account of fair valuation (as deemed cost) of items of PP&E and intangible assets (on convergence date) and of investments in subsidiaries, joint ventures and associates (on transition date), sold during the year	XXX
Add / less: adjustment to "other equity" on transition date on account of cumulative translation differences of a foreign operation, sold during the year	XXX
Add / less: adjustments on account of distribution of non-cash assets to shareholders in a demerger	XXX
Add / less: 1/5th of all other adjustments to "other equity" on convergence date	XXX
Add / less: other adjustments required as per Explanation 1 to Section 115JB(2) of the Income-tax Act, 1961	XXX

Key takeaways for CFOs

As companies published their first Ind AS annual financial statements, Ind AS is now a reality. With significant efforts already spent in effective transition to Ind AS, the path ahead may still require vital efforts on an ongoing basis. As evident from the analysis in this publication, there exist various inconsistencies and unexplained positions, which we believe would be ironed or clarified as companies move.

After this first public reporting, we believe CFOs have access to sufficient information on Ind AS adjustments made by industry peers. This should give companies an opportunity to further refine application of Ind AS including modification of key systems and processes for a consistent reporting system under Ind AS.

Road ahead for CFOs

Re-assess and review Ind AS impacts based on peers' reported results

For companies yet to report their first Ind AS compliant results, a study of Ind AS impacts on peer group or sector is a good reference point. On the other hand, for companies that had taken tentative accounting positions for reporting their first Ind AS results, there could still be a need to re-assess their positions based on their sector peers.

Identify 'what if' scenarios and stay informed

Companies may consider it necessary to create 'what if' scenarios, to identify transactions with varying Ind AS convergence outcomes based on their substance over form or for evaluating potential impacts on their balance sheet that is yet to be reported.

Tax considerations

There exist noticeable differences in accounting for transactions for preparation of financial statements under Ind AS and their tax implications. This has two-fold implications on companies:

a MAT is driven by book profits and Ind AS adjustments may lead to a direct impact on tax payouts for large section of companies.

b For companies falling in normal tax regime, ICDS provides limited or no guidance on accounting for several types of transactions, thereby leaving ambiguity in how those transactions are treated for tax purpose by companies vis-à-vis the view that tax authorities may eventually take.

IT System changes

Companies need to fine tune their systems for building reliable and consistent Ind AS reporting system.

Building capabilities

For a majority of companies who reported their Ind AS results in the nick of time, lack of knowledge of their financial reporting staff may have been a significant bottleneck in implementation of the new accounting standards. Companies will have to chalk out a strategy for enhancing the skill sets of their human resources by facilitating necessary technical trainings and till such time those skills are enhanced, rely on external support for ensuring true and fair financial reporting.

Glossary

Term	Description
ARO	Asset Retirement Obligation
BOOT	Build, Own, Operate, Transfer
BOT	Build, Operate, Transfer
ECL	Expected Credit Losses
EIR	Effective Interest Rate
ESOP	Employee Stock Option Scheme
FCMI	Foreign Currency Monetary Item
FDI	Foreign Direct Investment
FVOCI	Fair Value through Other Comprehensive Income
FVTPL	Fair Value through Profit and Loss
GAAP	Generally Accepted Accounting Principles
IASB	International Accounting Standards Board
ICAI	Institute of Chartered Accountants of India
ICDS	Income Computation and Disclosure Standards
IFRS	International Financial Reporting Standards
Ind AS	Indian Accounting Standards
MAT	Minimum Alternate Tax
MCA	Ministry of Corporate Affairs
MTM	Mark to Market
NBFC	Non-Banking Finance Companies
NCI	Non-Controlling Interest
OCI	Other Comprehensive Income
PP&E	Property, Plant and Equipment
PPP	Public Private Partnership
SCA	Service Concession Agreement

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