Educational Material on Indian Accounting Standard (Ind AS) 27, Separate Financial Statements & Indian Accounting Standard (Ind AS) 28, Investment in Associates and Joint Ventures

The Institute of Chartered Accountants of India
(Set up by an Act of Parliament)
New Delhi

Educational Material on Indian Accounting Standard (Ind AS) 27 Separate Financial Statements & Indian Accounting Standard (Ind AS) 28 Investments in Associates and Joint Ventures

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This Educational Material has been formulated in accordance with the Ind AS notified by the Ministry of Corporate Affairs (MCA) as Companies (Indian Accounting Standards) Rules, 2015 vide Notification dated February 16, 2015 and other amendments finalised and notified till March 2018.

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Foreword

With a view to achieve international benchmarks of financial reporting, the Institute of Chartered Accountants of India (ICAI), played a proactive role in formulating and implementing Indian Accounting Standards (Ind AS) converged with the International Financial Reporting Standards (IFRS). Ind AS has become a reality now as both Phase I and Phase II companies have implemented and published/or are publishing their financial results in accordance with Ind AS. The Ind AS Implementation Group of ICAI is playing an active role in educating the members and providing the guidance on practical issues that are being faced by the members and other stakeholders.

As a step in this direction, the Ind AS Implementation Group came out with this Educational Material covering Ind AS 27, *Separate Financial Statements* and Ind AS 28, *Investment in Associates and Joint Ventures.* The purpose of this Educational Material is to provide guidance by way of Frequently Asked Questions (FAQs) which explain the principles enunciated in the Standards. This publication will provide guidance to the stakeholders in how an entity accounts for the investments in its subsidiaries, associates and joint ventures.

I sincerely acknowledge the untiring efforts and support of CA. Nihar Niranjan Jambusaria, Convenor, CA. Dhinal Ashvinbhai Shah, Deputy Convenor as well as convenor of the Study Group and other members of the Ind AS Implementation Group for their valuable technical contribution and cooperation. I also congratulate CA. S. B. Zaware, Chairman and CA. M. P. Vijay Kumar, Vice-chairman, Accounting Standards Board for their support. I am sure that this Educational Material will be useful for all who are implementing Ind AS and also for those who will audit the financial statements in accordance with Ind AS.

I am of the firm belief that all these efforts of Ind AS Implementation Group will play a crucial role in smooth & effective implementation of Ind AS in India.

New Delhi | **CA. Naveen N.D. Gupta**

June 25, 2018 | ***President, ICAI***

Preface

Ind AS has become a reality now in the country with Phase I and Phase II companies which have already implemented Ind AS. The Institute of Chartered Accountants of India (ICAI) through its Ind AS Implementation Group is playing a pivotal role to ensure that Ind AS are implemented in the same spirit in which these have been formulated. For this purpose, the Ind AS Implementation Group is working to provide guidance to the members and other stakeholders by issuing Educational Materials on Ind AS, issuing timely clarifications on issues being faced by the members through Ind AS Technical Facilitation Group (ITFG) Clarification Bulletins, addressing queries through Support-desk for implementation of Ind AS, conducting Certificate Course on Ind AS, developing e-learning modules on Ind AS, workshops, seminars, awareness programmes on Ind AS and series of webcasts on Ind AS etc.

We are delighted that the Group has brought out this Educational Material covering Indian Accounting Standard (Ind AS) 27, *Separate Financial Statements* and Ind AS 28, *Investment in Associates and Joint Ventures*. Ind AS 27 prescribes the accounting and disclosure requirements for investments in subsidiaries, joint ventures and associates when an entity prepares separate financial statements and Ind AS 28 set out how to determine if an investment is an associate and prescribes the use of the equity method of accounting for investments in associates and joint ventures. This Educational Material contains summary of Ind AS 27 and Ind AS 28 discussing the key requirements of the Standards and the Frequently Asked Questions (FAQs) covering the issues, which are expected to be encountered frequently while implementing these Standards.

We may mention that the views expressed in this publication are the views of the Ind AS Implementation Group and are not necessarily the views of the Council of the Institute. The purpose of this publication is to provide guidance for implementing this Ind AS effectively by explaining the principles enunciated in the Standard with the help of examples. However, while applying Ind AS in a practical situation, reference should be made to the full text of the Standards.

We would like to convey sincere gratitude to our Hon'ble President, CA. Naveen N D Gupta and Vice-President, CA. Prafulla Premsukh Chhajed for providing us this opportunity of bringing out implementation guidance on Ind AS in the form of Educational Materials. We sincerely appreciate the efforts put in by CA. Sandip Khetan, Co-convenor and members of the Group CA. Archana Bhutani, CA. Deepa Dev, CA. Rohit Kumar, CA. Sanjeev Kumar and CA. Amit Jain for preparing the draft of this Educational Material. We would also like to thank all the members of the Ind AS Implementation Group for their valuable & technical contributions in finalising this publication.

We sincerely appreciate CA. Geetanshu Bansal, Secretary, Ind AS Implementation Group and CA. Prachi Jain, Executive Officer for their technical and administrative support in bringing out this publication. We would also like to thank CA. Vidhyadhar Kulkarni, Head, Technical Directorate, for his guidance.

We are sure that this Educational Material will be of great help in understanding the provisions of Ind AS 27 & Ind AS 28 and in their practical implementation.

CA. Nihar Niranjan Jambusaria
Convenor
Ind AS Implementation Group

CA. Dhinal Ashvinbhai Shah
Deputy convenor
Ind AS Implementation Group

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Educational Material on Indian Accounting Standard (Ind AS) 27 *Separate Financial Statements*

I. Ind AS 27 – Summary

Objective

To prescribe the accounting and disclosure requirements for investments in subsidiaries, joint ventures and associates when an entity prepares separate financial statements.

Scope

Ind AS 27 does not mandate which entities produce separate financial statements. It applies only when an entity prepares separate financial statements that comply with Indian Accounting Standards.

Key Definitions

Consolidated financial statements are the financial statements of a group in which the assets, liabilities, equity, income, expenses and cash flows of the parent and its subsidiaries are presented as those of a single economic entity.

Separate financial statements are those presented by a parent (i.e. an investor with control of a subsidiary) or an investor with joint control of, or significant influence over, an investee, in which the investments are accounted for at cost or in accordance with Ind AS 109, *Financial Instruments*.

Separate financial statements are those presented in addition to consolidated financial statements or in addition to financial statements in which investments in associates or joint ventures are accounted for using the equity method, other than in the following circumstances:

(a) An entity may present separate financial statements as its only financial statements if:

  (i) it is a wholly-owned subsidiary or is a partially-owned subsidiary of another entity and all its other owners, including those not otherwise entitled to vote, have been informed about, and do not object to, the parent not presenting consolidated financial statements;

(ii) its debt or equity instruments are not traded in a public market;

(iii) it did not file, nor is it in the process of filing, its financial statements with a securities commission or other regulatory organisation for the purpose of issuing any class of instruments in a public market; and

(iv) its ultimate or any intermediate parent produces financial statements that are available for public use and comply with Ind ASs, in which subsidiaries are consolidated or are measured at fair value through profit or loss in accordance with this Ind AS.

(b) A parent entity which is an investment entity is exempted from presenting the consolidated financial statements. Such entity is required to measure its investments in its subsidiaries at fair value, with changes in fair value recognised through profit or loss for each period, unless that subsidiary is not itself an investment entity and whose main purpose and activities are providing services that relate to the parent's investment activities, in which case the financial statements of the subsidiary are consolidated.

Preparation of separate financial statements

When an entity prepares separate financial statements, it shall account for investments in subsidiaries, joint ventures and associates either at cost, or in accordance with Ind AS 109, *Financial Instruments.*

The entity is required to apply the same accounting for each category of investments. However, when investments are classified as held for sale (or included in a disposal group that is classified as held for sale), they are accounted for at cost and shall be accounted for in accordance with Ind AS 105, *Non-current Assets Held for Sale and Discontinued Operations*. The measurement of investments accounted for in accordance with Ind AS 109 is not changed in such circumstances.

The cost option is not available in the following situations:

(i) When an investment in an associate or a joint venture is held by, or is held indirectly through, an entity that is a venture capital organisation, or a mutual fund, unit trust and similar entities including investment-linked insurance funds and an entity elects, to measure such investments at fair value through profit or loss in accordance with Ind AS 109, it shall also account for those investments in the same way in its separate financial statements..

(ii) Similarly, if a parent is required to measure its investment in a subsidiary at fair value through profit or loss as per the requirements of other Ind AS, it shall also account for its investment in a subsidiary in the same way in its separate financial statements.

Accounting Treatment in case when there is change of status in investment entities

(i) When an entity (parent) ceases to be an investment entity

When an entity ceases to be an investment entity, it shall account for the change from the date when the change in status occurred, the entity shall, either:

(a) account for an investment in a subsidiary at cost. The fair value of the subsidiary at the date of the change of status shall be used as the deemed cost at that date; or

(b) continue to account for an investment in a subsidiary in accordance with Ind AS 109.

(ii) When an entity (parent) becomes an investment entity

When an entity becomes an investment entity, it shall account for an investment in a subsidiary at fair value through profit or loss in accordance with Ind AS 109.

The difference between the previous carrying amount of the subsidiary and its fair value at the date of the change of status of the investor shall be recognised as a gain or loss in profit or loss.

The cumulative amount of any fair value adjustment previously recognised in other comprehensive income in respect of those subsidiaries shall be treated as if the investment entity had disposed of those subsidiaries at the date of change in status.

Dividend

An entity shall recognise a dividend from a subsidiary, a joint venture or an associate in profit or loss in its separate financial statements when its right to receive the dividend is established.

Accounting Treatment – When a parent reorganises the structure of its group

When a parent reorganises the structure of its group by establishing a new entity as its parent in a manner that satisfies the following criteria:

(a) the new parent obtains control of the original parent by issuing equity instruments in exchange for existing equity instruments of the original parent;

(b) the assets and liabilities of the new group and the original group are the same immediately before and after the reorganisation; and

(c) the owners of the original parent before the reorganisation have the same absolute and relative interests in the net assets of the original group and the new group immediately before and after the reorganisation.

In such cases, the new parent accounts for its investment in the original parent at cost in its separate financial statements.

Further, the new parent shall measure cost at the carrying amount of its share of the equity items shown in the separate financial statements of the original parent at the date of the reorganisation.

Similarly, an entity that is not a parent might establish a new entity as its parent in a manner that satisfies the above mentioned criteria. The above requirements apply equally to such reorganisations.

Disclosure

An entity shall apply all applicable Ind AS when providing disclosures in its separate financial statements.

When an investment entity that is a parent prepares separate financial statements as its only financial statements, it shall disclose in those separate financial statements:

(a) fact that the financial statements are separate financial statements.

(b) the disclosures relating to investment entities required by Ind AS 112, *Disclosure of Interests in Other Entities*.

When a parent, elects not to prepare consolidated financial statements and instead prepares separate financial statements, it shall disclose in those separate financial statements:

(a) the fact that the financial statements are separate financial statements; that the exemption from consolidation has been used; the name and principal place of business (and country of incorporation, if different) of the entity whose consolidated financial statements that comply with Ind ASs have been produced for public use; and the address where those consolidated financial statements are obtainable.

(b) a list of significant investments in subsidiaries, joint ventures and associates, including:

  (i) the name of those investees.

  (ii) the principal place of business (and country of incorporation, if different) of those investees.

  (iii) its proportion of the ownership interest (and its proportion of the voting rights, if different) held in those investees.

(c) a description of the method used to account for the investments listed under (b).

When a parent other than a parent electing not to prepare consolidated financial statements or an investor with joint control of, or significant influence over, an investee prepares separate financial statements, the parent or investor shall identify the financial statements prepared in accordance with Ind AS 110, Ind AS 111 or Ind AS 28 to which they relate. The parent or investor shall also disclose in its separate financial statements:

(a) the fact that the statements are separate financial statements.

(b) a list of significant investments in subsidiaries, joint ventures and associates, including:

  (i) the name of those investees.

  (ii) the principal place of business (and country of incorporation, if different) of those investees.

  (iii) its proportion of the ownership interest (and its proportion of the voting rights, if different) held in those investees.

(c) a description of the method used to account for the investments listed under (b).

II. Frequently Asked Questions

Scope

Question 1

Whether the investment entity is required to measure its investment in subsidiaries at fair value through profit or loss in its separate financial statements?

Response

Paragraph 11A of Ind AS 27, *Separate Financial Statements* provides that, “if a parent is required, in accordance with paragraph 31 of Ind AS 110, to measure its investment in a subsidiary at fair value through profit or loss in accordance with Ind AS 109, it shall also account for its investment in a subsidiary in the same way in its separate financial statements”.

In this regard, the requirements of paragraphs 31 and 32 of Ind AS 110, *Consolidated Financial Statements*, are as follows-

> “31 Except as described in paragraph 32, an investment entity shall not consolidate its subsidiaries or apply Ind AS 103 when it obtains control of another entity. Instead, an investment entity shall measure an investment in a subsidiary at fair value through profit or loss in accordance with Ind AS 109”.
>
> 32 Notwithstanding the requirement in paragraph 31, if an investment entity has a subsidiary that is not itself an investment entity and whose main purpose and activities are providing services that relate to the investment entity’s investment activities, it shall consolidate that subsidiary in accordance with paragraphs 19–26 of this Ind AS and apply the requirements of Ind AS 103 to the acquisition of any such subsidiary.”

Further as per paragraph 4B of Ind AS 110,“a parent that is an investment entity shall not present consolidated financial statements if it is required, in accordance with paragraph 31 of this Ind AS, to measure all of its subsidiaries at fair value through profit or loss”.

In accordance with the above requirements, the parent that is an investment entity is required to measure its investments in its subsidiaries (except for entities covered under paragraph 32 of Ind AS 110) at fair value through profit or loss in its consolidated financial statements as per the requirement of Ind AS 109. Further, such investment entity is required to account for these investments in the similar way in its separate financial statements as they have been accounted for in consolidated financial statements.

Question 2

A company, AB Ltd. holds investments in subsidiaries and associates. In its separate financial statements, AB Ltd. wants to elect to account its investments in subsidiaries at cost and the investments in associates as financial assets at fair value through profit or loss (FVTPL) in accordance with Ind AS 109, *Financial Instruments*.

Whether AB Limited can carry investments in subsidiaries at cost and investments in associates in accordance with Ind AS 109 in its separate financial statements?

Response

Paragraph 10 of Ind AS 27, *Separate Financial Statements inter-alia* provides that, when an entity prepares separate financial statements, it shall account for investments in subsidiaries, joint ventures and associates either at cost, or in accordance with Ind AS 109, *Financial Instruments* in its separate financial statements. Further, the entity shall apply the same accounting for each category of investments.

It may be noted that although the 'category' is used in number of Standards, it is not defined in any of the Ind AS. It seems that subsidiaries, associates and joint ventures would qualify as separate categories. Thus, the same accounting policies are applied for each category of investments - i.e. each of subsidiaries, associates and joint ventures. However, paragraph 10 of Ind AS 27 should not be read to mean that, in all circumstances, all investments in associates are one 'category' of investment and all investments in joint ventures or an associate are one 'category' of investment. These categories can be further divided into sub-categories provided the sub-category can be defined clearly and objectively and results in information that is relevant and reliable. For example, an investment entity parent can have investment entity subsidiary (at fair value through profit or loss) and non-investment entity subsidiary (whose main purpose is to provide services that relate to the investment entity's investment activities) as separate categories in its separate financial statements.

In the present case, investment in subsidiaries and associates are considered to be different categories of investments. Further, Ind AS 27 requires to account for the investment in subsidiaries, joint ventures and associates either at cost, or in accordance with Ind AS 109 for each category of Investment. Thus, AB Limited can carry its investments in subsidiaries at cost and its investments in associates as financial assets in accordance with Ind AS 109 in its separate financial statements.

Question 3

AB Limited has an existing investment of INR 700 crores in its subsidiary, PQR Limited. The net assets of PQR limited are only INR 400 crores as at March 31, 2018. The value in use as well as fair value less costs to sell of PQR Limited is INR 600 crores.

AB Limited has accounted its subsidiary at cost in its financial statements.

What will be the impairment loss which AB Limited needs to recognise in the separate financial statements?

Response

The relevant definitions given under paragraph 6 of Ind AS 36, *Impairment of Assets* are as follows:

Carrying amount is the amount at which an asset is recognised after deducting any accumulated depreciation (amortisation) and accumulated impairment losses thereon.

Impairment loss is the amount by which the carrying amount of an asset or a cash-generating unit exceeds its recoverable amount.

Recoverable amount of an asset or a cash-generating unit is the higher of its fair value less costs of disposal and its value in use.

Value in use is the present value of the future cash flows expected to be derived from an asset or cash-generating unit.

Paragraph 59 of Ind AS 36 provides that, "if, and only if, the recoverable amount of an asset is less than its carrying amount, the carrying amount of the asset shall be reduced to its recoverable amount. That reduction is an impairment loss".

Further, paragraph 61 of Ind AS 36, *inter alia*, provides that, an impairment loss on a non-revalued asset is recognised in profit or loss.

In accordance with the above, in the instant case, impairment loss of Rs. 100 crores shall be recognised in the statement of profit and loss. However, it is also important to consider the underlying cash flows that support the investment while considering the investment for impairment.

Question 4

A parent entity A Ltd. has elected to account for its investments in its subsidiary at FVTPL in accordance with Ind AS 109, *Financial Instruments*. As a result, it measures its investments at fair value at each reporting date. However, A Ltd. is unable to reliably measure the fair value of one of its subsidiaries, Subsidiary B, which was set up an year ago and is not quoted on an active market.

Does the fact that the fair value of one subsidiary cannot be measured reliably preclude A Ltd. from carrying its other subsidiaries at fair value in its separate financial statements?

Response

Paragraph 10 of Ind AS 27, *Separate Financial Statements, inter alia,* states that, "when an entity prepares separate financial statements, it shall account for investments in subsidiaries, joint ventures and associates either:

(a) at cost, or

(b) in accordance with Ind AS 109.

The entity shall apply the same accounting for each category of investments".

Further, paragraphs B5.2.3–B5.2.6 of Ind AS 109, *Financial Instruments* provide as follows:

B5.2.3 All investments in equity instruments and contracts on those instruments must be measured at fair value. However, in limited circumstances, cost may be an appropriate estimate of fair value. That may be the case if insufficient more recent information is available to measure fair value, or if there is a wide range of possible fair value measurements and cost represents the best estimate of fair value within that range.

B5.2.4 Indicators that cost might not be representative of fair value includes:

a) a significant change in the performance of the investee compared with budgets, plans or milestones.

b) changes in expectation that the investee's technical product milestones will be achieved.

c) a significant change in the market for the investee's equity or its products or potential products.

d) a significant change in the global economy or the economic environment in which the investee operates.

e) a significant change in the performance of comparable entities, or in the valuations implied by the overall market.

f) internal matters of the investee such as fraud, commercial disputes, litigation, changes in management or strategy.

g) evidence from external transactions in the investee's equity, either by the investee (such as a fresh issue of equity), or by transfers of equity instruments between third parties.

B5.2.5 The list in paragraph B5.2.4 is not exhaustive. An entity shall use all information about the performance and operations of the investee that becomes available after the date of initial recognition. To the extent that any such relevant factors exist, they may indicate that cost might not be representative of fair value. In such cases, the entity must measure fair value.

B5.2.6 Cost is never the best estimate of fair value for investments in quoted equity instruments (or contracts on quoted equity instruments).

On the basis of above, if an entity has elected to account for its investments in its subsidiary at FVTPL in accordance with Ind AS 109, then all such investments should be measured at fair value in accordance with Ind AS 109. However, in very limited circumstances, cost may be an appropriate estimate of fair value (for example, where insufficient recent information is available to determine fair value, or where there is a wide range of possible fair value measurements and cost represents the best estimate of fair value within that range). It may be noted that such circumstances would never apply to equity investments held by particular entities such as financial institutions and investment funds.

Under Ind AS 109, investments in equity instruments can be carried at cost only if either of the conditions stated above is met. Further while Ind AS 109 provides an exemption, it is expected to be available only in limited circumstances. It is acknowledged that current observable prices would usually not be available for unlisted companies. However, in such cases, instead of considering cost as a default measurement basis, fair value should be determined using unobservable inputs.

It is important to note that use of cost as per B5.2.3 does not refer to use of cost method; instead it only recognises that cost is an approximate of fair value in limited circumstances. For assessing whether or not cost is representative of fair value, in addition to considering the factors in B5.2.4 (stated above), an investor considers the existence of factors such as whether the environment in which the investee operates is dynamic, whether there have been changes in market conditions and the passage of time. Such factors might undermine the appropriateness of using cost as a means of measuring the fair value of unquoted equity instruments at the measurement date.

For assessing whether cost is an approximation of fair value, all facts and circumstances need to be considered carefully. As stated above, usually, current observable prices for shares in private companies are not available. In such case, the measurement of fair value is based on valuation techniques that use unobservable inputs (generally classified as Level 3 in the fair value hierarchy). There is no exemption from use of fair value in case fair value cannot be measured reliably. This seems to be on the basis that given the extensive and comprehensive guidance in Ind AS 113, *Fair Value Measurement,* fair value can be determined reliably for unlisted entities.

In the given case, the entity should determine the fair value as per guidance provided in Ind AS 109. Only if, after following the guidance of Ind AS 109, A Ltd. concludes that cost is an approximate of fair value of its investment in subsidiary B, the Company can use the cost as its deemed fair value.

Question 5

Whether a company is required to disclose the fact that the financial statements prepared by them are separate financial statements?

Response

(i) *When the separate financial statements are prepared by a parent company that elects not to present consolidated financial statements,* then in accordance with paragraph 16(a) of Ind AS 27, it is required to disclose in those separate financial statements, the fact that the financial statements are separate financial statements.

(ii) *When separate financial statements are prepared by an investment entity* as its only financial statements in accordance with paragraph 16A of Ind AS 27, then it is required to disclose that fact in the financial statements.

(iii) *When the separate financial statements are prepared by a parent (other than (i) and (ii) above) or by an investor with joint control of, or significant influence over, an investee,* the parent or investor shall identify the financial statements prepared in accordance with Ind AS 110, Ind AS 111 or Ind AS 28 to which they relate. In accordance with paragraph 17 (a) of Ind AS 27, it is also required to disclose in those separate financial statements, the fact that the financial statements are separate financial statements.

Therefore, in all the above cases, the companies are required to disclose in its separate financial statements the fact that the financial statements prepared by them are separate financial statements.

Appendix I

Issues addressed in ITFG Clarification Bulletins

Post Ind AS adoption accounting treatment of profit share from investment in limited liability partnership which is under joint control (in separate financial statements)

***Issue 1*: Company A Ltd. has equity investment in a Limited Liability Partnership (LLP). Company A Ltd. has joint control over the LLP and assessed that investment in LLP is a joint venture. How investment in LLP be accounted for in the separate financial statements of Company A Ltd? Whether profit share from LLP will be adjusted to the carrying amount of the investment in LLP in the separate financial statements of Company A Ltd.?**

***Response*:** Paragraph 26 of Ind AS 111, *Joint Arrangements,* prescribes the accounting treatment for investment in joint arrangements in separate financial statement of joint operator or joint venture as follows:

"26 In its separate financial statements, a joint operator or joint venturer shall account for its interest in:

(a) a joint operation in accordance with paragraph 20-22;

(b) a joint venture in accordance with paragraph 10 of Ind AS 27, Separate Financial Statements."

Paragraph 10 of Ind AS 27, *Separate Financial Statements*, *inter alia*, provides that when an entity prepares separate financial statements, it shall account for investments in subsidiaries, joint ventures and associates either:

(a) at cost, or

(b) in accordance with Ind AS 109.

In the given case, Company A Ltd. has joint control over the LLP and has assessed that investment in LLP is a joint venture. Accordingly, the entity shall account for its investment in the joint venture in its separate financial statements as per paragraph 10 of Ind AS 27, i.e. at cost or in accordance with Ind AS 109. Therefore, adjustment of profit share from LLP to the carrying amount of the investment in LLP in its separate financial statements is not permitted.

The accounting of return on investment (i.e. profit share from LLP) will depend on the terms of contract between Company A Ltd. and LLP. The share in profit in LLP shall be recognised as income in the statement of profit and loss as and when the right to receive its profit share is established.

(ITFG Clarification Bulletin 5, Issue 8)
(Date of finalisation: September 19, 2016)

Measurement of investment in subsidiaries at cost if valued at fair value on date of transition

***Issue 2*: Company A has made investment in subsidiary S Ltd. Company A elects to measure the investment in S Ltd. at fair value on the date of transition as per Ind AS 101. Can Company A opt to carry the investment in S Ltd. at cost after the date of transition as per Ind AS 27?**

***Response*:** Paragraph D15 of Ind AS 101, *First-time Adoption of Indian Accounting Standards* states as under:

"If a first-time adopter measures such an investment at cost in accordance with Ind AS 27, it shall measure that investment at one of the following amounts in its separate opening Ind AS Balance Sheet:

(a) cost determined in accordance with Ind AS 27; or

(b) deemed cost. The deemed cost of such an investment shall be its:

  (i) fair value at the entity's date of transition to Ind ASs in its separate financial statements; or

  (ii) previous GAAP carrying amount at that date.

A first-time adopter may choose either (i) or (ii) above to measure its investment in each subsidiary, joint venture or associate that it elects to measure using a deemed cost."

Further, paragraph 10 of Ind AS 27, *Separate Financial Statements, inter-alia,* states as under:

"When an entity prepares separate financial statements, it shall account for investments in subsidiaries, joint ventures and associates either:

(a) at cost, or

(b) in accordance with Ind AS 109."

In accordance with the above, it may be noted that for a first-time adopter cost of investment in a subsidiary shall be one of the following amounts:

- cost determined in accordance with Ind AS 27 (i.e. retrospective application of Ind AS 27)
- fair value at the entity's date of transition to Ind AS
- previous GAAP carrying amount

Accordingly, if a company chooses to measure its investment at fair value at the date of transition then that is deemed to be cost of such investment for the company and, therefore, it shall carry its investment at that amount (i.e. fair value at the date of transition) after the date of transition.

Accordingly, in the given case, Company A can carry investment in S Ltd. at transition date fair value which is deemed to be its cost as per paragraph 10 of Ind AS 27.

(ITFG Clarification Bulletin 3, Issue 12)
(Date of finalisation: June 22, 2016)

Appendix II

Note: The purpose of this Appendix is only to bring out the major differences, if any, between Indian Accounting Standard (Ind AS) 27 and the corresponding International Accounting Standard (IAS) 27, Separate Financial Statements, issued by the International Accounting Standards Board.

Major differences between Ind AS 27, *Separate Financial Statements* and IAS 27, *Separate Financial Statements*

1. IAS 27 requires to disclose the reason for preparing separate financial statements if not required by law. In India, since the Companies Act mandates preparation of separate financial statements, such requirement has been removed in Ind AS 27.

2. IAS 27 allows the entities to use the equity method to account for investment in subsidiaries, joint ventures and associates in their Separate Financial Statements (SFS). This option is not given in Ind AS 27, as the equity method is not a measurement basis like cost and fair value but is a manner of consolidation and therefore would lead to inconsistent accounting conceptually.

Educational Material on Indian Accounting Standard (Ind AS) 28

Investments in Associates and Joint Ventures

Educational Material on Indian Accounting Standard (Ind AS) 28 *Investments in Associates and Joint Ventures*

I. Ind AS 28 – Summary

Objective

To prescribe the accounting for investments in associates and requirements for the application of the equity method when accounting for investments in associates and joint ventures.

Scope

This Standard shall be applied by all entities that are investors with joint control of, or significant influence over, an investee.

Key Requirements of Ind AS 28

An associate is an entity over which the investor has significant influence.

Significant influence is the power to participate in the financial and operating policy decisions of the investee but is **not control** or **joint control** of those policies.

Joint control is the contractually agreed sharing of control of an arrangement, which exists only when decisions about the relevant activities require the unanimous consent of the parties sharing control.

Significant influence

When an entity holds, directly or indirectly (e.g. through subsidiaries), 20 per cent or more of the voting power of the investee, it is presumed that the entity has significant influence. However, in case the investor clearly demonstrates that the holding does not give significant influence over investee then this would not apply. Conversely, if the entity holds, directly or indirectly (e.g. through subsidiaries), less than 20 per cent of the voting power of the investee, it is presumed that the entity does not have significant influence. In such case, if the investor clearly demonstrates that the holding gives it a significant influence over the investee then this would not apply. A substantial or majority ownership by another investor does not necessarily preclude an entity from having significant influence.

The existence of significant influence by an entity is usually evidenced in one or more of the following ways:

(a) representation on the board of directors or equivalent governing body of the investee;

(b) participation in policy-making processes, including participation in decisions about dividends or other distributions;

(c) material transactions between the entity and its investee;

(d) interchange of managerial personnel; or

(e) provision of essential technical information.

The existence and effect of potential voting rights that are currently exercisable or convertible, including potential voting rights held by other entities, are considered when assessing whether an entity has significant influence. In making this assessment the entity examines all facts and circumstances that affect potential rights, except the intentions of management and the financial ability to exercise or convert those potential rights.

An entity loses significant influence over an investee when it loses the power to participate in the financial and operating policy decisions of that investee. The loss of significant influence can occur with or without a change in absolute or relative ownership levels. It could occur, for example, when an associate becomes subject to the control of a government, court, administrator or regulator. It could also occur as a result of a contractual arrangement.

Application of the equity method

An entity with joint control of, or significant influence over, an investee shall account for its investment in an associate or a joint venture using the equity method except when that investment qualifies for exemption.

Equity method

Under the equity method, on initial recognition the investment in an associate or a joint venture is recognised at cost, and the carrying amount is increased or decreased to recognise the investor's share of the profit or loss of the investee after the date of acquisition. The investor's share of the investee's profit or loss is recognised in the investor's profit or loss. Distributions received from an investee reduce the carrying amount of the investment. Adjustments to the carrying amount may also be necessary for changes in the investor's proportionate interest in the investee arising from changes in the investee's other comprehensive income.

When potential voting rights exist, an entity's interest in an associate or a joint venture is determined solely on the basis of existing ownership interests and does not reflect the possible exercise or conversion of potential voting rights unless an entity has, in substance, an existing ownership as a result of a transaction that currently gives it access to the returns associated with an ownership interest. In such circumstances, the proportion allocated to the entity is determined by taking into account the eventual exercise of those potential voting rights and other derivative instruments that currently give the entity access to the returns.

Equity method procedures

A group's share in an associate or a joint venture is the aggregate of the holdings in that associate or joint venture by the parent and its subsidiaries. The holdings of the group's other associates or joint ventures are ignored for this purpose.

The entity's financial statements shall be prepared using uniform accounting policies for like transactions and events in similar circumstances unless, in case of an associate, it is impracticable to do so. If accounting policies other than those of the entity are being used for like transactions and events in similar circumstances, adjustments shall be made to make the associate's or joint venture's accounting policies conform to those of the entity for applying the equity method. However, if an entity that is not itself an investment entity has an interest in an associate or joint venture that is an investment entity, the entity may, when applying the equity method, elect to retain the fair value measurement applied by that investment entity associate or joint venture to the investment entity associate's or joint venture's interests in subsidiaries.

The most recent available financial statements of the associate or joint venture are used by the entity in applying the equity method. When the end of the reporting period of the entity is different from that of the associate or joint venture, the associate or joint venture prepares, for the use of the entity, financial statements as of the same date as the financial statements of the entity unless it is impracticable to do so. Adjustments shall be made for the effects of significant transactions or events that occur between that date and the date of the entity's financial statements. In any case, the difference between the end of the reporting period of the associate or joint venture and that of the entity shall be no more than three months.

An investment is accounted for using the equity method from the date on which it becomes an associate or a joint venture. On acquisition of the investment, any difference between the cost of the investment and the entity's share of the net fair value of the investee's identifiable assets and liabilities is accounted for as follows:

(a) Goodwill relating to an associate or a joint venture is included in the carrying amount of the investment. Amortisation of that goodwill is not permitted.

(b) Any excess of the entity's share of the net fair value of the investee's identifiable assets and liabilities over the cost of the investment is recognised directly in equity as capital reserve in the period in which the investment is acquired.

Appropriate adjustments to the entity's share of the associate's or joint venture's profit or loss after acquisition are made in order to account, for example, for depreciation of the depreciable assets based on their fair values at the acquisition date. Similarly, appropriate adjustments to the entity's share of the associate's or joint venture's profit or loss after acquisition are made for impairment losses such as for goodwill or property, plant and equipment.

Exemptions from applying the equity method

An entity need not apply the equity method to its investment in an associate or a joint venture if the entity is a parent that is exempt from preparing consolidated financial statements by the scope exception in Ind AS 110 or if all the following apply:

(a) The entity is a wholly-owned subsidiary, or is a partially-owned subsidiary of another entity and its other owners, including those not otherwise entitled to vote, have been informed about, and do not object to, the entity not applying the equity method.

(b) The entity's debt or equity instruments are not traded in a public market.

(c) The entity did not file, nor is it in the process of filing, its financial statements with a securities commission or other regulatory organisation, for the purpose of issuing any class of instruments in a public market.

(d) The ultimate or any intermediate parent of the entity produces financial statements available for public use that comply with Ind ASs, in which subsidiaries are consolidated or are measured at fair value through profit or loss in accordance with Ind AS 110.

When an investment in an associate or a joint venture is held by, or is held indirectly through, an entity that is a venture capital organisation, or a mutual fund, unit trust and similar entities including investment-linked insurance funds, the entity may elect to measure that investment at fair value through profit or loss in accordance with Ind AS 109. An entity shall make this election separately for each associate or joint venture, at initial recognition of the associate or joint venture.

When a portion of the investment is held indirectly through a venture capital organisation, or a mutual fund, unit trust and similar entities including investment-linked insurance funds, the entity may elect to measure that portion of the investment at fair value through profit or loss in accordance with Ind AS 109 regardless of whether the venture capital organisation has significant influence over that portion of the investment and shall apply equity method to any remaining portion of its investment in an associate that is not held through a venture capital organisation.

Classification as held for sale

An entity shall apply Ind AS 105 to an investment or a portion of an investment in an associate or a joint venture that meets the criteria to be classified as held for sale. Any retained portion that has not been classified as held for sale shall be accounted for using the equity method until disposal of the portion that is classified as held for sale takes place. After the disposal takes place, any retained interest in the associate or joint venture shall be accounted for in accordance with Ind AS 109 unless the retained interest continues to be an associate or a joint venture, in which case the entity uses the equity method.

When an investment or a portion of an investment previously classified as held for sale no longer meets the criteria to be so classified, it shall be accounted for using the equity method retrospectively as from the date of its classification as held for sale. Financial statements for the periods since classification as held for sale shall be amended accordingly.

Discontinuing the use of the equity method

An entity shall discontinue the use of the equity method from the date when its investment ceases to be an associate or a joint venture as follows:

(a) If the investment becomes a subsidiary, the entity shall account for its investment in accordance with Ind AS 103, *Business Combinations*, and Ind AS 110, *Consolidated Financial Statements*.

(b) If the retained interest in the former associate or joint venture is a financial asset, the entity shall measure the retained interest at fair value. The entity shall recognise in profit or loss any difference between:

  (i) the fair value of any retained interest and any proceeds from disposing of a part interest in the associate or joint venture; and

  (ii) the carrying amount of the investment at the date the equity method was discontinued.

(c) When an entity discontinues the use of the equity method, the entity shall account for all amounts previously recognised in other comprehensive income in relation to that investment on the same basis as would have been required if the investee had directly disposed off the related assets or liabilities.

If gain or loss previously recognised in other comprehensive income by the investee would be reclassified to profit or loss on the disposal of the related assets or liabilities, the entity reclassifies the gain or loss from equity to profit or loss (as a reclassification adjustment) when the equity method is discontinued.

If an investment in an associate becomes an investment in a joint venture or an investment in a joint venture becomes an investment in an associate, the entity continues to apply the equity method and does not remeasure the retained interest.

Changes in ownership interest

If an entity's ownership interest in an associate or a joint venture is reduced, but the entity continues to apply the equity method, the entity shall reclassify to profit or loss the proportion of the gain or loss that had previously been recognised in other comprehensive income relating to that reduction in ownership interest if that gain or loss would be required to be reclassified to profit or loss on the disposal of the related assets or liabilities.

Impairment losses

After application of the equity method, including recognising the associate's or joint venture's losses, the entity applies the requirements of Ind AS 109, *Financial Instruments* to determine whether it is necessary to recognise any additional impairment loss with respect to its net investment in the associate or joint venture.

The net investment in an associate or joint venture is impaired and impairment losses are incurred only in that condition when-

- there is objective evidence of impairment as a result of one or more events that occurred after the initial recognition of the net investment (a 'loss event'); and
- that loss event (or events) has an impact on the estimated future cash flows from the net investment that can be reliably estimated.

It may not be possible to identify a single, discrete event that caused the impairment. Rather the combined effect of several events may have caused the impairment.

Because goodwill that forms part of the carrying amount of the net investment in an associate or a joint venture is not separately recognised, it is not tested for impairment separately by applying the requirements for impairment testing goodwill in Ind AS 36, *Impairment of Assets*. Instead, the entire carrying amount of the investment is tested for impairment in accordance with Ind AS 36 as a single asset, by comparing its recoverable amount (higher of value in use and fair value less costs to sell) with its carrying amount, whenever it is indicated that the net investment may be impaired.

Separate financial statements

An investment in an associate or a joint venture shall be accounted for in the entity's separate financial statements either at cost or in accordance with Ind AS 109.

No disclosures are specified in this Standard as Ind AS 112, *Disclosure of Interests in Other Entities* deals with the disclosures required for entities with joint control of, or significant influence over, an investee.

Frequently Asked Questions

Note: It is presumed in all the FAQs that the entity has significant influence if the shareholding exceeds 20% voting rights, unless otherwise specified.

Significant Influence

Question 1

Whether voting rights on shares held by nominee or in a fiduciary capacity are considered while evaluating the significant influence of beneficiary shareholder over the investee?

Response

Paragraph 5 of Ind AS 28, *inter alia*, provides that, "if an entity holds, directly or indirectly (e.g. through subsidiaries), 20 per cent or more of the voting power of the investee, it is presumed that the entity has significant influence, unless it can be clearly demonstrated that this is not the case".

Voting rights on shares held by nominee should be considered while evaluating the significant influence of beneficiary shareholder over the investee but not for the evaluation of significant influence by the nominee shareholder over the investee as such voting rights are exercised by the nominee as per the directions and in interest of the beneficiary.

Further, the Ministry of Corporate Affairs vide general circular no. 24/2014, dated 25.06.2014 clarified that the shares held by a company in another company in a 'fiduciary capacity' shall not be counted for the purpose of determining the relationship of 'associate company' under section 2(6) of the Companies Act, 2013.

Therefore, beneficiary shareholder shall consider the voting rights on shares held by its nominee or in a fiduciary capacity while evaluating the significant influence over the investee.

Question 2

Whether restrictions on transfer of funds from the investee to the entity preclude the existence of significant influence of entity over the investee?

Response

Paragraph 9 of Ind AS 28 states that, "an entity loses significant influence over an investee when it loses the power to participate in the financial and operating policy decisions of that investee. The loss of significant influence can occur with or without a change in absolute or relative ownership levels. It could occur, for example, when an associate becomes subject to the control of a government, court, administrator or regulator. It could also occur as a result of a contractual arrangement."

There is difference on account of applicability of equity accounting under AS 23 and Ind AS 28. AS 23 provides an exemption from applying equity method when the associate operates under severe long-term restrictions that significantly impair its ability to transfer funds to the investor. Such investments shall be accounted for in accordance with AS 13. However, no such exemption is provided under Ind AS 28.

In the current scenario, an investor with an interest in such an associate should evaluate the facts and circumstances to assess whether it is still able to exercise significant influence over the financial and operating policies of the investee.

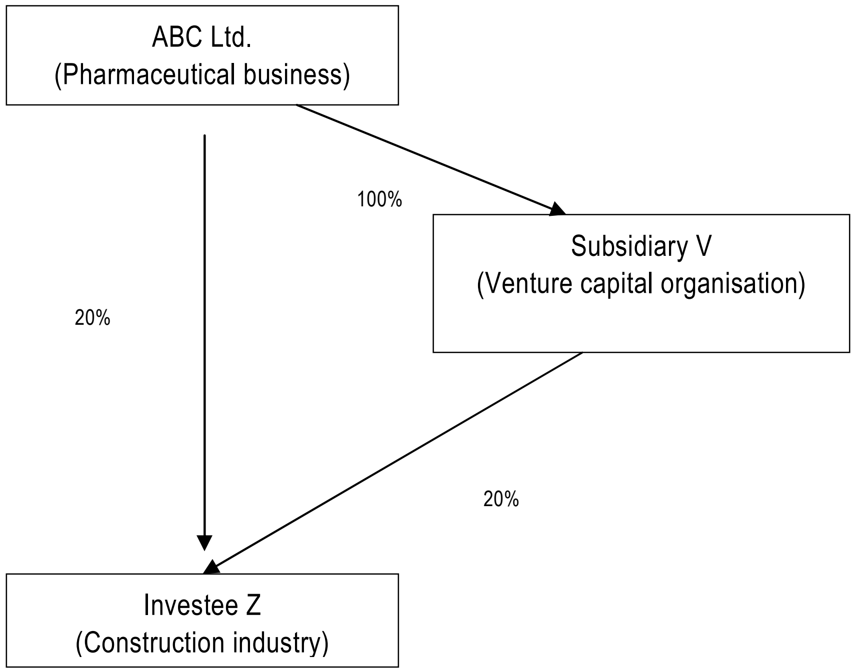
However, such restrictions do not, in isolation, preclude the exercise of significant influence. Long-term restrictions on a stand-alone basis ordinarily may not result in the impairment of significant influence but this combined with other factors as mentioned in Ind AS 28 may hamper the ability of the entity to demonstrate significant influence.

Accordingly, when assessing its ability to exercise significant influence over an entity, an investor should consider severe long-term restrictions on the transfer of funds from the associate to the investor, along with other factors as mentioned under Ind AS 28.

Application of the equity method

Question 3

ABC Ltd. operates a pharmaceutical business and owns a venture capital organisation (subsidiary V) that invests in the construction industry. V's business is monitored on the basis of the fair value of its investments. ABC Ltd. and V hold 20% shares each in an investee Z. How shall ABC Ltd. account for its investment (directly and indirectly through V) in the investee Z in its consolidated financial statements?



Response

Paragraph 18 of Ind AS 28 states that, "when an investment in an associate or a joint venture is held by, or is held indirectly through, an entity that is a venture capital organisation, or a mutual fund, unit trust and similar entities including investment-linked insurance funds, the entity may elect to measure investments in those associates and joint ventures at fair value through profit or loss in accordance with Ind AS 109. An entity shall make this election separately for each associate or joint venture, at initial recognition of the associate or joint venture".

Paragraph 19 of Ind AS 28 further includes that "when an entity has an investment in an associate, a portion of which is held indirectly through a venture capital organisation, or a mutual fund, unit trust and similar entities including investment-linked insurance funds, the entity may elect to measure that portion of the investment in the associate at fair value through profit or loss in accordance with Ind AS 109 regardless of whether the venture capital organisation has significant influence over that portion of the investment. If the entity makes that election, the entity shall apply the equity method to any remaining portion of its investment in an associate that is not held through a venture capital organisation".

In the instant case, even though the entity ABC Ltd. itself is not a venture capital organisation, its subsidiary V would be able to apply the exemption and account for its investments at fair value through profit or loss in accordance with Ind AS 109. Therefore, in the consolidated financial statements of the ABC Ltd.:

- the investments held indirectly through V i.e. 20% shares of the investee, may be accounted either at fair value under Ind AS 109, with changes in fair value recognised in profit or loss in the period of change or as per equity method accounting; and
- the investments held by the entity directly in Z should be accounted for using equity method accounting.

Question 4

An entity P (parent) has two wholly-owned subsidiaries - X and Y, each of which has an ownership interest in an 'associate', entity Z. Subsidiary X is a venture capital organisation. Neither of the investments held in associate Z by subsidiaries X and Y is held for trading. Subsidiary X and Y account for their investment in associate Z at fair value through profit or loss in accordance with Ind AS 109 and using the equity method in accordance with Ind AS 28 respectively.

How should P account for the investment in associate Z in the following scenarios:

Scenario 1: Where both investments in the associate result in significant influence on a stand-alone basis - Subsidiary X and Y ownership interest in associate Z is 25% and 20% respectively.

Scenario 2: When neither of the investments in the associate results in significant influence on a stand-alone basis, but do provide the parent with significant influence on a combined basis - Subsidiary X and Y ownership interest in associate Z is 10% each.

Scenario 3: When one of the investments in the associate results in significant influence on a stand-alone basis and the other investment in the associate does not result in significant influence on a stand-alone basis - Subsidiary X and Y ownership interest in associate Z is 30% and 10% respectively.

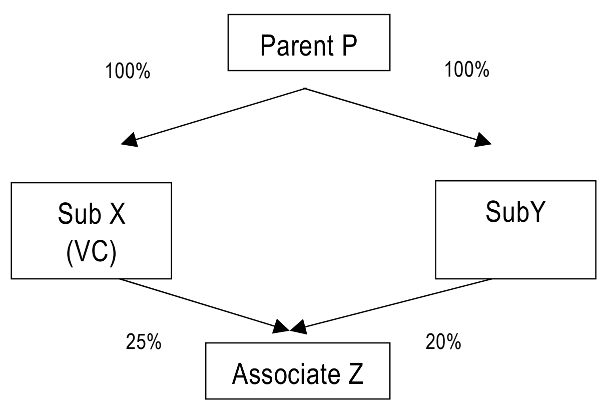
Assume there is significant influence if the entity has 20% or more voting rights.

Response

Paragraph 18 of Ind AS 28 states that, "when an investment in an associate or a joint venture is held by, or is held indirectly through, an entity that is a venture capital organisation, or a mutual fund, unit trust and similar entities including investment-linked insurance funds, the entity may elect to measure investments in those associates and joint ventures at fair value through profit or loss in accordance with Ind AS 109. An entity shall make this election separately for each associate or joint venture, at initial recognition of the associate or joint venture."

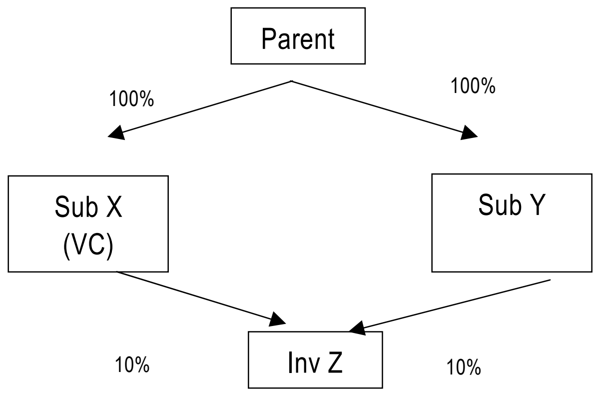
Paragraph 19 of Ind AS 28 provides that, "'when an entity has an investment in an associate, a portion of which is held indirectly through a venture capital organisation, or a mutual fund, unit trust and similar entities including investment-linked insurance funds, the entity may elect to measure that portion of the investment in the associate at fair value through profit or loss in accordance with Ind AS 109 regardless of whether the venture capital organisation has significant influence over that portion of the investment. If the entity makes that election, the entity shall apply the equity method to any remaining portion of its investment in an associate that is not held through a venture capital organisation". Therefore, fair value exemption can be applied partially in such cases.

Scenario 1: Where both investments in the associate result in significant influence on a stand-alone basis.



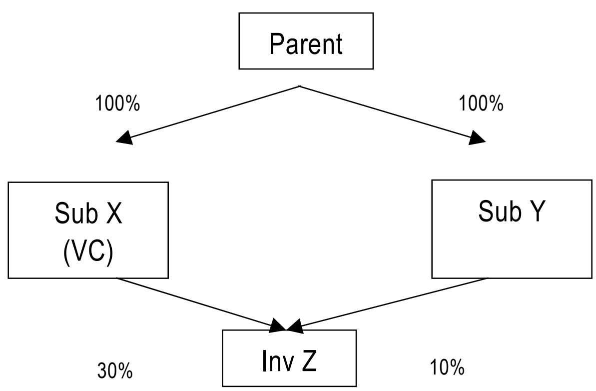
In the present case, in accordance with paragraph 19 of Ind AS 28, P must follow equity method of accounting for its 20% interest held by Y. Under the partial use of fair value exemption, P may elect to measure the 25% interest held by X at fair value through profit or loss.

Scenario 2: When neither of the investments in the associate results in significant influence on a stand-alone basis, but do provide the parent with significant influence on a combined basis.



In the present case in accordance with the paragraph 19 of Ind AS 28, P must follow equity method of accounting for its 10% interest held by Y, even though Y would not have significant influence on a stand-alone basis. Under the partial use of fair value exemption, P may elect to measure the 10% interest held by X at fair value through profit or loss.

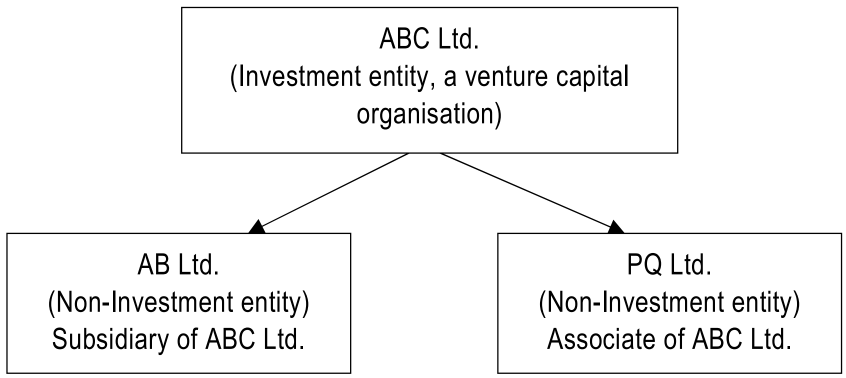
Scenario 3: When one of the investments in the associate results in significant influence on a stand-alone basis and the other investment in the associate does not result in significant influence on a stand-alone basis



In the present case, in accordance with paragraph 19 of Ind AS 28, P must follow equity method of accounting for its 10% interest held by Y, even though Y would not have significant influence on a stand-alone basis. Under the partial use of fair value exemption, the P may elect to measure the 30% interest held by X at fair value through profit or loss.

Question 5

Following is the group structure of ABC Limited:



ABC Limited is a venture capital organisation and fulfils the definition of investment entity under Ind AS 110, *Consolidated Financial Statements*.

How should ABC Limited account for its investment in AB Limited and PQ Limited in its financial statements under Ind AS 110 and Ind AS 28?

Response

Paragraph 18 of Ind AS 28 provides that, "when an investment in an associate or a joint venture is held by, or is held indirectly through, an entity that is a venture capital organisation, or a mutual fund, unit trust and similar entities including investment-linked insurance funds, the entity may elect to measure investments in those associates or joint ventures at fair value through profit or loss in accordance with Ind AS 109. An entity shall make this election separately for each associate or joint venture, at initial recognition of the associate or joint venture".

This is an exemption from the requirement to measure interests in joint ventures and associates using the equity method, rather than an exception to the scope of Ind AS 28 for the equity accounting for joint ventures and associates held by these entities. Thus, such entities may elect to measure their investments in associates or joint ventures at fair value through profit or loss (FVTPL) as per Ind AS 109.

Further, paragraph 4B read with paragraphs 31 and 32 of Ind AS 110 provides an exception to an investment entity from the presentation of consolidated financial statements and requires such entities to measure the subsidiaries at FVTPL, unless the subsidiary itself is not an investment entity and whose main purpose and activities are providing services that relate to the investment entity's investment activities, in which case it shall consolidate such subsidiary.

Thus, Ind AS 110 requires entities that meet the definition of an investment entity to measure investments in subsidiaries at FVTPL. The application of the investment entity exception is not an accounting policy choice. If an entity meets the definition of an investment entity, it is required to measure its subsidiaries at fair value through profit or loss.

Paragraph 27 of Ind AS 110, *inter alia,* states that an investment entity is an entity that measures and evaluates the performance of substantially all of its investments on a fair value basis; this is one of the elements of the definition of investment entity. Paragraph 85K(a) of Ind AS 110 states that in order to demonstrate that it meets this element of the definition, an investment entity provides investors with fair value information and measures substantially all of its investments at fair value in its financial statements whenever fair value is required or permitted in accordance with Ind ASs.

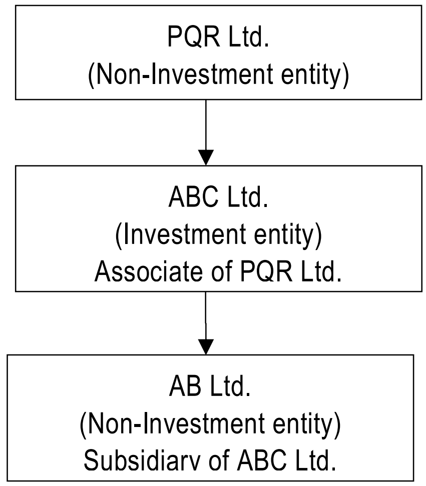
Further, as per paragraph B85L of Ind AS 110, in order to meet the requirement in B85K(a), an investment entity would elect the exemption from applying the equity method in Ind AS 28 for its investments in associates and joint ventures and measure its financial assets at fair value using the requirements in Ind AS 109.

In view of above, while paragraph 18 of Ind AS 28 gives an option to a venture capital organisation, or a mutual fund, unit trust and similar entities including investment-linked insurance funds to measure investments in associate either by applying equity method or at fair value through profit or loss, such an option would need to be necessarily exercised by such entities in order to meet the definition of an investment entity. To qualify as an investment entity, such entities are required to measure its investment in associates at fair value through profit or loss as required under paragraph B85L of Ind AS 110.

In view of above, ABC Limited in the instant case, shall measure both its subsidiary AB Limited and associate PQ Limited at FVTPL.

Question 6

Following is the group structure of PQR Limited:



What shall be the requirements of application of equity method accounting by PQR Limited and consolidation requirements by ABC Limited under Ind AS 28 and Ind AS 110 respectively?

Response

In the present case, PQR Limited has an associate, ABC Limited which is an investment entity. As per Ind AS 28, PQR Limited shall apply equity method of accounting to its investment in its associate, ABC Limited.

Paragraph 36 of Ind AS 28 states that, "except as described in paragraph 36A, if an associate or a joint venture uses accounting policies other than those of the entity for like transactions and events in similar circumstances, adjustments shall be made to make the associate's or joint venture's accounting policies conform to those of the entity when the associate's or joint venture's financial statements are used by the entity in applying the equity method".

Paragraph 36A further provides that "notwithstanding the requirement in paragraph 36, if an entity that is not itself an investment entity has an interest in an associate or joint venture that is an investment entity, the entity may, when applying the equity method, elect to retain the fair value measurement applied by that investment entity associate or joint venture to the investment entity associate's or joint venture's interests in subsidiaries. This election is made separately for each investment entity associate or joint venture, at the later of the date on which (a) the investment entity associate or joint venture is initially recognised; (b) the associate or joint venture becomes an investment entity; and (c) the investment entity associate or joint venture first becomes a parent".

Accordingly, Ind AS 28 provides choice to the non-investment parent to retain the fair values applied by investment entity associate to its investment in subsidiaries. At a standalone entity level, such investment entity parent is mandatorily required to measure the subsidiaries at fair value through profit and loss (FVTPL), unless the subsidiary that is not itself an investment entity provides services that relate to the investment entity's investment activities.

Thus, in the instant case, ABC Limited, an investment entity parent has an exception from the presentation of consolidated financial statements and shall mandatorily measure its investment in AB Limited at FVTPL in view of paragraphs 4B, 31 and 32 of Ind AS 110.

PQR Limited, non-investment entity, however has a choice to either retain the fair values applied by ABC Limited associate to its investment in AB Limited or make adjustments to conform the accounting policy followed by ABC Limited to those used by PQR Limited.

Question 7

An entity A owns 100% shares of the investee company X which were originally purchased for Rs.700 crores and had incurred directly attributable cost of Rs.50 crores.

Entity A sells 60% of the shares in the company X to Entity B for Rs.1,500 crores. As a result of the sale, Entity B obtains control over company X. Entity A retains 40% interest and determines that it has significant influence over company X.

At the date of disposal, the fair value of the identifiable assets and liabilities of company X including intangible assets is Rs. 1,800 crores and the fair value of Entity A's retained interest of 40% of the shares of Company X is Rs. 800 crores, which includes goodwill.

How entity A should measure the initial carrying amount of the investment in company X following disposal of its 60% interest?

Response

Paragraph 25 of Ind AS 110, *inter-alia*, states that, "if a parent loses control of a subsidiary the parent recognises any investment retained in the former subsidiary at its fair value when control is lost and subsequently accounts for it and for any amounts owed by or to the former subsidiary in accordance with relevant Ind ASs. That fair value shall be regarded as the fair value on initial recognition of a financial asset in accordance with Ind AS 109 or, when appropriate, the cost on initial recognition of an investment in an associate or joint venture".

Accordingly, in the given case, upon loss of control, entity A should deconsolidate the Company X and account for its remaining interest in Company X, as an associate or joint venture using the equity method of accounting. Entity A's initial carrying amount of the associate should be based on the fair value of the retained interest, i.e. Rs.800 crores.

The analysis of investment in Company X is as follows:

(Rs in crores)

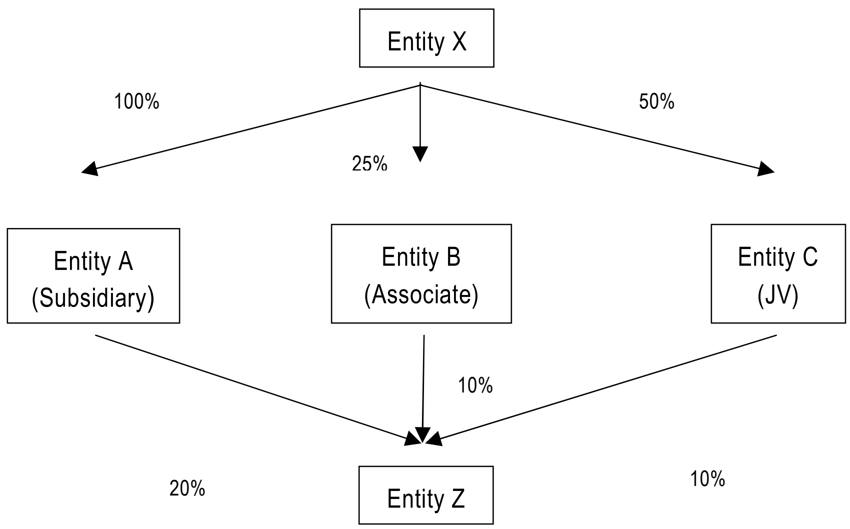
Goodwill	Identifiable net assets	Total Investment in Company X
80[1]	720[2]	800

Note 1: Calculation of Goodwill: 800 –720 = 80

Note 2: Calculation of identifiable net assets: 720= 40% of Rs. 1,800 , i.e., fair value of the identifiable assets and liabilities of the Company X.

Question 8

An entity X holds 100% investment in subsidiary A, which in turn holds a 20% investment in associate Z. In addition, entity X also holds a 25% investment in associate B and a 50% investment in joint venture C, each of which holds a 10% investment in associate Z.



What shall be the entity X's share in entity Z?

Response

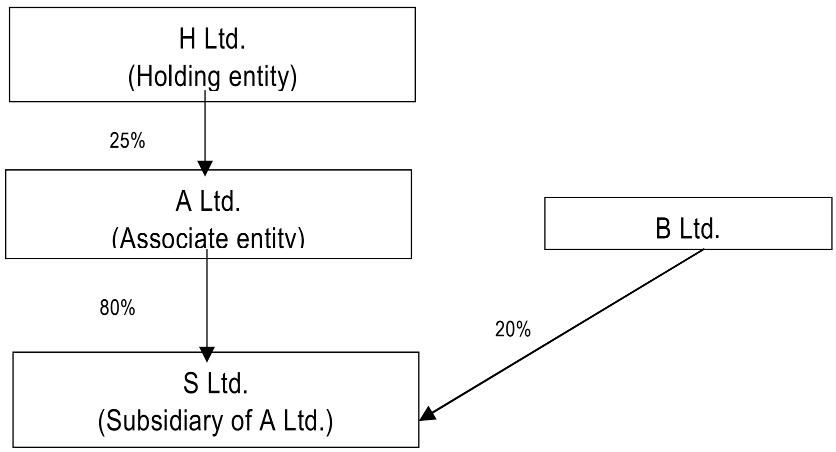
Paragraph 27 of Ind AS 28, *inter-alia,* states that, "a group's share in an associate or a joint venture is the aggregate of the holdings in that associate or joint venture by the parent and its subsidiaries. The holdings of the group's other associates or joint ventures are ignored for this purpose".

Therefore, in its consolidated financial statements entity X accounts for a 20% investment in associate Z under the equity method because:

- the investments in associate Z held by associate B and joint venture C should not be taken into account; and
- entity X fully consolidates the assets of its subsidiary A, which include a 20% investment in associate Z. Entity X should consolidate such 20% holding in entity Z under equity method.

Question 9

Following is the structure of H Limited:



Whether H Ltd. should base the accounting for its share of the associate or joint venture's profits, other comprehensive income and net assets under the equity method on the amounts before or after non-controlling interests in the associate or joint venture's consolidated accounts ?

Response

Paragraph 27 of Ind AS 28, *inter-alia*, states that, "when an associate or a joint venture has subsidiaries, associates or joint ventures, the profit or loss, other comprehensive income and net assets taken into account in applying the equity method are those recognised in the associate's or joint venture's financial statements (including the associate's or joint venture's share of the profit or loss, other comprehensive income and net assets of its associates and joint ventures), after any adjustments necessary to give effect to uniform accounting policies".

In certain cases, it might be possible that the associate or joint venture does not own all the shares in some of its subsidiaries, in which case its consolidated financial statements will include non-controlling interests.

Paragraph 22 of Ind AS 110, *Consolidated Financial Statements*, provides that, "a parent shall present non-controlling interests in the consolidated balance sheet within equity, separately from the equity of the owners of the parent". Further, paragraphs B94-B96 of Ind AS 110 provide guidance in this regard.

The profit or loss and other comprehensive income reported in the associate or joint venture's consolidated financial statements will include 100% of the amounts relating to the subsidiaries, but the overall profit or loss and total comprehensive income will be split between the amounts attributable to the owners of the parent (i.e. the associate or joint venture) and those attributable to the non-controlling interests. The net assets in the consolidated balance sheet will also include 100% of the amounts relating to the subsidiaries, with any non-controlling interests in the net assets presented within the consolidated balance sheet within equity, separately from the equity of the owners of the parent.

For such cases, Ind AS 28 does not explicitly address whether the investor should base the accounting for its share in the profits, other comprehensive income and net assets of its associate or joint venture under the equity method on the amounts before or after any non-controlling interests in the associate or joint venture's consolidated accounts. However, as the investor's interest in the associate or joint venture is as an owner of the parent, the share is based on the profit or loss, comprehensive income and equity (net assets) that are reported as being attributable to the owners of the parent in the associate or joint venture's consolidated financial statements, i.e. after any amounts attributable to the non-controlling interests.

Accordingly, the H Ltd. should base the accounting for its share in profits, other comprehensive income and net assets of A Ltd. and B Ltd. under equity method of accounting on the amounts after non-controlling interests in A Ltd's consolidated accounts.

Question 10

How should transactions between the reporting entity and its associates or joint ventures be eliminated at the time of applying equity method of consolidation?

Response

Paragraph 28 of Ind AS 28 states that, "gains and losses resulting from 'upstream' and 'downstream' transactions between an entity (including its consolidated subsidiaries) and its associate or joint venture are recognised in the entity's financial statements only to the extent of unrelated investors' interests in the associate or joint venture. 'Upstream' transactions are, for example, sales of assets from an associate or a joint venture to the investor. 'Downstream' transactions are, for example, sales or contributions of assets from the investor to its associate or its joint venture. The investor's share in the associate's or joint venture's gains or losses resulting from these transactions is eliminated".

The following approach might be used to apply the above guidance provided under Ind AS:

— in the statement of profit or loss, the adjustment should be taken against either the investor's profit or the share of the associate's or joint venture's profit, according to whether the investor or the associate or joint venture recorded the profit on the transaction, respectively; and

— in the balance sheet, the adjustment should be made against the asset which was the subject of the transaction if it is held by the investor or against the carrying amount for the associate or joint venture if the asset is held by the associate or joint venture.

This is consistent with the approach required by paragraph 30 of Ind AS 28 which deals with the elimination of unrealised gains and losses arising on contributions of non-monetary assets to an associate or joint venture in exchange for an equity interest in the associate or joint venture. It explains that such unrealised gains and losses shall be eliminated against the investment accounted for using the equity method and shall not be presented as deferred gains or losses in the entity's consolidated balance sheet or in the entity's balance sheet in which investments are accounted for using the equity method.

Question 11

How should goodwill / capital reserve be computed on step increase in an existing associate / joint venture? Is there a need for re-measurement of existing ownership interest at the time of the increase?

Response

An entity may acquire an additional interest in an existing associate or joint venture that continues to be an associate or joint venture accounted for under the equity method. Ind AS 28 doesn't provide explicit guidance for such transaction. Paragraph 10 of Ind AS 28 which deals with initial recognition of investment requires that on initial recognition the investment in an associate or a joint venture is recognised at cost, and the carrying amount is increased or decreased to recognise the investor's share of the profit or loss of the investee after the date of acquisition.

Paragraph 32 of Ind AS 28 states that, "an investment is accounted for using the equity method from the date on which it becomes an associate or a joint venture. On acquisition of the investment, any difference between the cost of the investment and the entity's share of the net fair value of the investee's identifiable assets and liabilities is accounted for as follows:

(a) Goodwill relating to an associate or a joint venture is included in the carrying amount of the investment. Amortisation of that goodwill is not permitted.

(b) Any excess of the entity's share of the net fair value of the investee's identifiable assets and liabilities over the cost of the investment is recognised directly in equity as capital reserve in the period in which the investment is acquired.

Appropriate adjustments to the entity's share of the associate's or joint venture's profit or loss after acquisition are made in order to account, for example, for depreciation of the depreciable assets based on their fair values at the acquisition date. Similarly, appropriate adjustments to the entity's share of the associate's or joint venture's profit or loss after acquisition are made for impairment losses such as for goodwill or property, plant and equipment".

The above paragraph establishes the requirement that the cost of investment in an associate or joint venture is allocated to the purchase of a share of the fair value of net assets and the goodwill. This requirement is not limited to the initial application of equity accounting, but applies to each acquisition of an investment. However, this does not result in any revaluation of the existing share of net assets.

Rather, the existing ownership interests are accounted for under paragraphs 10 and 32 of Ind AS 28, whereby the carrying value is adjusted only for the investor's share of the associate or joint venture's profits or losses and other recognised equity transactions. No entry is recognised to reflect changes in the fair value of assets and liabilities that are not recognised under the accounting policies applied for the associate or joint venture.

Hence, the purchase price paid for the additional interest should be added to the existing carrying amount of the associate or the joint venture and the existing interest in the associate or joint venture should not be remeasured. The additional interest acquired should be notionally split between goodwill and the additional interest in the fair value of the net assets of the associate or joint venture. This split is based on the fair value of the net assets at the date of the increase in the associate or joint venture. However, no remeasurement should be made for previously unrecognised changes in the fair values of identifiable net assets.

Therefore, goodwill / capital reserve will be computed based on fair value of identified assets and liabilities on the date of further acquisition.

To demonstrate, an entity X obtains significant influence over entity Y by acquiring an investment of 20% at a cost of Rs.2,00,000. At the date of the acquisition of the investment, the fair value of the associate's net identifiable assets is Rs. 9,50,000. The investment is accounted for under the equity method in the consolidated financial statements of entity X.

Subsequently, entity X acquires an additional investment of 15% in entity Y at a cost of Rs.1,80,000, increasing its total investment in entity Y to 35%. There is no change in the status of investee, the investment is however, still an associate and accounted for using the equity method of accounting and the current fair value of the associate's net identifiable assets has increased to Rs. 10,00,000.

Assuming no directly attributable cost has been incurred and no profit / loss arose during the period since the acquisition of first 20%.

In this case, the carrying amount of the investment immediately prior to the additional investment is Rs.2,00,000.

Upon acquisition of additional 15% the equity-accounted amount for the associate increases by Rs.1,80,000. The notional goodwill applicable to the second tranche of the acquisition is Rs. 30,000 [Rs. 1,80,000 – (15% × Rs. 10,00,000)].

The impact of the additional investment on Entity A's equity-accounted amount for Entity B is summarised as follows:

Particulars	% held	Carrying amount	Share of net assets	Goodwill included in investment*
		Rs.	Rs.	Rs.
Existing investment	20%	2,00,000	1,90,000	10,000
Additional investment	15%	1,80,000	1,50,000	30,000

Total investment	**35%**	**380,000**	**340,000**	**40,000**

** For the purpose of simplicity, we have assumed that the difference pertains to goodwill only. However, in certain cases, it may also pertain to other intangible assets as well. Accordingly, an entity is required to evaluate and identify whether there is any other intangible asset. It has also been assumed that the company has not earned or incurred any profit or loss.*

Question 12

Whether the financial statements of an associate which is prepared as on a date subsequent to the reporting date of an entity, can be used for the purpose of applying the equity method of accounting under Ind AS 28?

Response

Paragraph 33 of Ind AS 28 provides that, "the most recent available financial statements of the associate or joint venture are used by the entity in applying the equity method. When the end of the reporting period of the entity is different from that of the associate or joint venture, the associate or joint venture prepares, for the use of the entity, financial statements as of the same date as the financial statements of the entity unless it is impracticable to do so".

Further, paragraph 34 of Ind AS 28 states that "when, in accordance with paragraph 33, the financial statements of an associate or a joint venture used in applying the equity method are prepared as of a date different from that used by the entity, adjustments shall be made for the effects of significant transactions or events that occur between that date and the date of the entity's financial statements. In any case, the difference between the end of the reporting period of the associate or joint venture and that of the entity shall be no more than three months. The length of the reporting periods and any difference between the ends of the reporting periods shall be the same from period to period".

The standard provides that when it is impracticable to prepare the financial statements of the associate as at the same date as the financial statements of the entity (investor), financials statements of the associate prepared for different reporting date may be used provided that length of the reporting periods and any difference between the ends of the reporting periods shall be the same from period to period i.e. consistently applied from period to period. Therefore, financial statements of an associate prepared as at a date subsequent to the reporting enterprise date can be used for the purpose of applying the equity method, provided the above consistency principle is not violated.

When financial statements with a different reporting date are used, adjustments are made for the effects of any significant events or transactions between the investor (or its consolidated subsidiaries) and the associate that occur between the date of the associate's financial statements and the date of the investor's consolidated financial statements.

It may be noted that generally in India the above situation of different reporting dates will not arise because of regulatory requirements such as timelines as prescribed by SEBI and other regulatory restrictions etc.

Question 13

An associate X holds 20% shares of another associate Y and associate Y holds 20% shares of associate X. The share capital of each of the associate is 100,000 shares at Rs. 10 each. X's profit excluding its share in Y = Rs. 100,000; Y's profit excluding its share in X = Rs. 100,000.

Considering the above facts, how would entity X and Y account for reciprocal holdings? Also, whether adjustment for the cross holdings is required to be made in the earnings per share calculation? It may be noted that X and Y are not venture capital organisations.

Response

Paragraph 26 of Ind AS 28 states that "Many of the procedures that are appropriate for the application of the equity method are similar to the consolidation procedures described in Ind AS 110. Furthermore, the concepts underlying the procedures used in accounting for the acquisition of a subsidiary are also adopted in accounting for the acquisition of an investment in an associate or a joint venture".

Paragraph 27 of Ind AS 28, *inter alia*, provides that, "when an associate or a joint venture has subsidiaries, associates or joint ventures, the profit or loss, other comprehensive income and net assets taken into account in applying the equity method are those recognised in the associate's or joint venture's financial statements (including the associate's or joint venture's share of the profit or loss, other comprehensive income and net assets of its associates and joint ventures), after any adjustments necessary to give effect to uniform accounting policies". This paragraph on literal reading suggests that an entity recognises its share of associate's profits including associate's equity accounted profits. However, in the case of reciprocal holdings this approach would result in a portion of entity's profits being double-counted as explained below:

In the instant case, X's profit (x) is dependent on Y's profit (y) and vice versa.

X's profit = Rs. 100,000 + 20% of Y's profit and similarly Y's profit = Rs. 100,000 + 20% of X's profit. However, the same shall result in X's profit being Rs. 125,000 and Y's profit being Rs.125,000, which is apparently leading to double counting of profit.

Therefore, it is considered appropriate in case of reciprocal holdings to adopt an approach of simply accounting for interest in associate i.e. 20% in the instant case (ignoring the reciprocal interest held by the associate i.e. before adding the reciprocal profit). This approach results in entity X and Y both recognising profit of Rs. 120,000. The difference of Rs. 5,000 (Rs. 125,000 - 120,000) represents the equity effect of the reciprocal holdings and therefore, the same is not recognised in the statement of profit & loss.

Further, the aforementioned paragraph 26 of Ind AS 28 supports the above approach since the equity method of accounting involves consolidation-type procedures that include elimination of unrealised profits. The analogy can be drawn from paragraph B86(c) of Ind AS 110 which prescribes that in consolidated financial statements the income arising on the investment held by a subsidiary in a parent is eliminated. Therefore, in applying consolidation procedures in equity accounting, income arising from associate's investment in the investor is also eliminated.

For the purpose of calculating the earnings per share the profits related to the reciprocal interests have been ignored. Therefore, it is necessary to adjust the number of shares to eliminate the reciprocal holdings while calculating the earnings per share.

For the purpose of earnings per share calculation, associate Y's ordinary shares are reduced to its effective holding i.e. 96,000. Entity Y indirectly owns 20% of X's 20% interest, i.e. entity Y indirectly owns 4% (= 20% × 20%) of its own shares. Those shares should therefore be treated as being equivalent to treasury shares and be ignored for the purposes of the EPS calculation.

This has been shown as below:

Particulars	Amount
Y's total share capital **(A)**	100,000
Share capital held by X in Y	20,000
Y's share in X (%)	20%
Y's share in X **(B)**	4,000
Y's share capital after excluding his interest (A - B)	**96,000**

On the similar basis, X's share capital after excluding his interest shall be Rs. 96,000.

Question 14

Whether appropriation to mandatory reserves be excluded from the results of operations of the associate that would be used for the purpose of computing the investor's share?

Response

Paragraph 3 of Ind AS 28 states that, "equity method is a method of accounting whereby the investment is initially recognised at cost and adjusted thereafter for the post-acquisition change in the investor's share of the investee's net assets. The investor's profit or loss includes its share of the investee's profit or loss and the investor's other comprehensive income includes its share of the investee's other comprehensive income".

The creation of such a reserve is merely appropriation of profits and doesn't result in reduction of the profit as well as net assets of the associate. Therefore, an entity should not exclude the appropriation made to mandatory reserves from the result of operations of the associate that would be used for the purpose of computing the investor's share.

For example, as per the terms of an agreement entered into with its debenture holders, an associate is required to appropriate adequate portion of its profits to a specified reserve over the period of maturity of the debentures such that, at the redemption date, the reserve constitutes at least half the value of such debentures. Although, such debenture appropriations are not available for distribution to the equity shareholders, however, entity should not exclude this from the computation of its share in the results of operations of the associate.

Question 15

Entity XYZ acquired a 10% interest in entity ABC for Rs. 100,000 at 1 June 2017. The investment in entity ABC was accounted for as equity investment (not held for trading) for which irrevocable option has been availed of routing the changes in fair value through other comprehensive income and related FVOCI reserve.

Entity XYZ recognised an increase in fair value of Rs. 60,000 in other comprehensive income for the year ended 31 March 2018.

Entity XYZ acquired an additional 25% interest in entity ABC for Rs. 4,00,000 at 1 April 2018 and achieved significant influence. The fair value of entity ABC's net assets was Rs. 500,000 at June 2017 and had increased to Rs. 800,000 at 1 April 2018.

Entity ABC recorded profits after dividends of Rs. 200,000 between 1 June 2017 and 1 April 2018.

How should an entity account for an investment in an investee on account of piece-meal acquisition when such investment provides it significant influence over the investee?

Response

An entity may gain significant influence or joint control over an existing investment upon acquisition of a further interest by way of piece-meal acquisition. Paragraph 26 of Ind 28 states that, "many of the procedures that are appropriate for the application of the equity method are similar to the consolidation procedures described in Ind AS 110. Furthermore, the concepts underlying the procedures used in accounting for the acquisition of a subsidiary are also adopted in accounting for the acquisition of an investment in an associate or a joint venture".

Paragraph 10 of Ind AS 28 requires while applying equity method, the investment in an associate is initially recognised at cost. However, it doesn't include any specific guidance on how an investor should account for an existing investment, which is accounted for under Ind AS 109, that subsequently becomes an associate or a joint venture that should be accounted for under the equity method.

However, paragraph 42 of Ind AS 103, *Business Combination*, deals with the situation where control over an acquiree is achieved in stages, the acquirer shall remeasure its previously held equity interest in the acquiree at its acquisition-date fair value and recognise the resulting gain or loss, if any, in profit or loss or other comprehensive income, as appropriate. In prior reporting periods, the acquirer may have recognised changes in the value of its equity interest in the acquiree in other comprehensive income. If so, the amount that was recognised in other comprehensive income shall be recognised on the same basis as would be required if the acquirer had disposed directly of the previously held equity interest.

Therefore, in the instant case, based on the above guidance an entity may account for the step acquisition of an associate or a joint venture by applying analogy to Ind AS 103, i.e. considering fair value as deemed cost. Accordingly, the cost of an associate acquired in stages is measured as the sum of the fair value of the interest previously held plus the fair value of any additional consideration transferred as of the date when the investment became an associate. Further, as per paragraph 42 of Ind AS 103, if an enity has previously recognised changes in the value of its equity interest in the acquiree in other comprehensive income, the amount that was recognised in other comprehensive income shall be recognised on the same basis as would be required if the acquirer had disposed directly of the previously held equity interest i.e. reclassified within equity.

The following shall be the accounting treatment

Particulars	**Amount**
Fair value of previous 10% interest held (determined by reference to the fair value of consideration given to acquire the additional 25%)* [400,000 / 25% *10%]	160,000
**Simplistic calculation has been used here only for the purpose of this illustration. The appropriateness of the method of measuring fair value should be evaluated on the basis of principles of Ind AS 113, Fair Value Measurement.*	
Fair value of additional 25% (amount paid)	4,00,000
	560,000

Goodwill is calculated as follows :

Cost of investment in associate	560,000
Fair value of identifiable net assets acquired (800,000*35%)	280,000

Goodwill	**280,000**

Journal entry:

(Rs.)

Particulars	Dr / Cr	Amount
Investment A/c (Including goodwill of Rs. 280,000)	Dr.	560,000
OCI (Equity)	Dr.	60,000
To Cash	Cr.	400,000
To Investment (FVOCI)	Cr.	160,000
To Retained earnings (Equity)	Cr.	60,000

Question 16

A Limited holds 25% interest in B Limited which is accounted for as investment in associate as per the equity method in the consolidated financial statements of A Limited. During the financial year ended March 2018, A Limited sold its 15% interest in B Limited to a third party X Limited for Rs. 80,000 and continues to hold 10% interest in B Limited as its financial asset. Carrying value of 25% investment in consolidated financial statements on the date of sale is Rs. 120,000 and fair value of retained interest is Rs. 65,000. Cumulative share of associate's other comprehensive income Rs. 20,000 represents exchange difference relating to a foreign operation.

How should this sale transaction and financial asset be accounted for in the financial statements of A Limited?

Response

Paragraph 22 of Ind AS 28 states as follows:

"An entity shall discontinue the use of the equity method from the date when its investment ceases to be an associate or a joint venture as follows:

(a) ....

(b) If the retained interest in the former associate or joint venture is a financial asset, the entity shall measure the retained interest at fair value. The fair value of the retained interest shall be regarded as its fair value on initial recognition as a financial asset in accordance with Ind AS 109. The entity shall recognise in profit or loss any difference between:

(i) the fair value of any retained interest and any proceeds from disposing of a part interest in the associate or joint venture; and

(ii) the carrying amount of the investment at the date the equity method was discontinued.

(c) When an entity discontinues the use of the equity method, the entity shall account for all amounts previously recognised in other comprehensive income in relation to that investment on the same basis as would have been required if the investee had directly disposed of the related assets or liabilities."

Further, paragraph 23 of Ind AS 28 states that, "therefore, if a gain or loss previously recognised in other comprehensive income by the investee would be reclassified to profit or loss on the disposal of the related assets or liabilities, the entity reclassifies the gain or loss from equity to profit or loss (as a reclassification adjustment) when the equity method is discontinued. For example, if an associate or a joint venture has cumulative exchange differences relating to a foreign operation and the entity discontinues the use of the equity method, the entity shall reclassify to profit or loss the gain or loss that had previously been recognised in other comprehensive income in relation to the foreign operation".

It is pertinent to note that the reclassification adjustment from equity to profit or loss is for the full amount that is in other comprehensive income and not just a proportionate amount based upon the interest disposed of. The loss of significant influence or joint control is a significant economic event that warrants accounting for the transaction as a disposal under Ind AS 21 and hence the transfer of the full exchange difference rather than just the proportionate share that would be required if this was accounted for as a partial disposal under Ind AS 21.

Accordingly, in the given case, the equity method earlier followed by the entity needs to be discontinued from the date of transfer of 15% interest in B Limited (that is, the date on which B Limited ceases to be an associate of A Limited) and the retained interest will be accounted for as a financial asset. The retained financial interest will be classified and measured as per the principals of Ind AS 109. At inception (date of transfer of 15% interest in B Limited), the retained interest will be measured at fair value, i.e. Rs. 65,000.

Any difference in fair value of any retained interest plus proceeds from disposal of 15% interest and the carrying amount of the investment at the date the equity method was discontinued will be recognised in profit and loss i.e. Rs. 25,000 (Rs. 65,000 + Rs. 80,000 - Rs. 120,000).

Furthermore, the entire share of associate's other comprehensive income of Rs.20,000 representing exchange difference relating to a foreign operation will be reclassified to profit or loss.

The accounting entry shall be as follows:

(i) Derecognition of investment in associate and recognition of retained interest at fair value

(Rs.)

Particulars	Dr / Cr	Amount
Investment in financial asset (10% stake)	Dr.	65,000
Cash on sale of investment	Dr.	80,000
To Investment in associate (carrying value)	Cr.	120,000
To Profit and loss	Cr.	25,000

(ii) Reclassifying from other comprehensive income to the statement of profit and loss

Particulars	Dr / Cr	Amount
OCI (Equity)	Dr.	20,000
To Profit and loss (reclassified as part of gain on partial disposal)	Cr.	20,000

Question 17

XYZ Ltd. has a 40% stake in its associate ABC Ltd. During the period, XYZ Ltd. sells 10% of its stake in ABC Ltd. for consideration of Rs. 80,000. From the date of the partial disposal, XYZ Ltd. will continue to recognise its remaining 30% interest in ABC Ltd. as an associate.

At the date of the partial disposal, the net asset carrying value of ABC Ltd. is Rs. 300,000. Goodwill was calculated at Rs. 30,000 at the date of acquiring the associate and there has been no impairment. Cumulative share of associate's other comprehensive income Rs. 20,000 represents actuarial gain or loss.

How to account for partial disposals of interests in associate or joint venture where the equity method continues to be applied?

Response

As per paragraph 25 of Ind AS 28, "If an entity's ownership interest in an associate or a joint venture is reduced, but the entity continues to apply the equity method, the entity shall reclassify to profit or loss the proportion of the gain or loss that had previously been recognised in other comprehensive income relating to that reduction in ownership interest if that gain or loss would be required to be reclassified to profit or loss on the disposal of the related assets or liabilities."

On such partial disposal, Ind AS 28 does not expressly deals with derecognition of proportionate investment in associate.

However, it is noted that the above reclassification of amounts from other comprehensive income to profit or loss is required as part of determining the gain or loss on disposal. Therefore, once ownership is reduced in cases of partial disposal, entity shall derecognise the carrying value of the associate proportionate to the percentage reduced and recognise the resulting gain or loss in profit and loss. Further, it shall reclassify the gain or losses previously recognised in other comprehensive income to the statement of profit and loss on proportionate basis.

In the instant case, the associate's carrying values in entity XYZ's consolidated financial statements is Rs. 150,000 [40% of 300,000 + 30,000]. Carrying value of associate proportionate to the percentage is reduced by Rs.37,500 (150,000 * 10/40).

The proportion of gain or loss previously recognised in OCI to be reclassified to profit or loss is Rs. 5000 (20,000/40%*10%)

Thus, the accounting entry shall be as follows:

i) On partial disposal of 10% stake

(Rs.)

Particulars	Dr / Cr	Amount
Cash	Dr.	80,000
To Investment in associate	Cr.	37,500

To Gain on partial disposal	Cr.	42,500

ii) Reclassifying from Other comprehensive to the statement of profit and loss on partial disposal

(Rs.)

Particulars	Dr / Cr	Amount
OCI (Equity)	Dr.	5,000
To Profit and loss (reclassified as part of gain on partial disposal)	Cr.	5,000
(20,000/40%*10%)		

Appendix I

Note: The purpose of this Appendix is only to bring out the major differences, if any, between Indian Accounting Standard (Ind AS) 28 and the corresponding International Accounting Standard (IAS) 28, Investments in Associates and Joint ventures, issued by the International Accounting Standards Board.

Major differences between Ind AS 28 *Investments in Associates and Joint ventures* and IAS 28, *Investments in Associates and Joint ventures*

(i) IAS 28 requires that for the purpose of applying equity method of accounting in the preparation of investor's financial statements, uniform accounting policies should be used. In other words, if the associate's accounting policies are different from those of the investor, the investor should change the financial statements of the associate by using same accounting policies. In Ind AS 28, the phrase, 'unless impracticable to do so' has been added in the paragraph 35 as certain associates, e.g., regional rural banks (RRBs), being associates of nationalized banks, are not in a position to use Ind AS as these may be too advanced for the RRBs. Accordingly, the above-stated words have been included to exempt such associates.

(ii) Ind AS 28 requires to transfer excess of the investor's share of the net fair value of the investee's identifiable assets and liabilities over the cost of investment in capital reserve whereas in IAS 28, it is recognised in profit or loss.

Appendix II

Note: The purpose of this Appendix is only to bring out the major differences, if any, between Indian Accounting Standard (Ind AS) 28, Investments in Associates and Joint ventures and the Accounting Standard (AS) 23, Accounting for Investments in Associates in Consolidated Financial Statements issued by the International Accounting Standards Board.

Major differences between Ind AS 28, *Investments in Associates and Joint ventures* and AS 23 (issued 2001), *Accounting for Investments in Associates in Consolidated Financial Statements*

(i) In AS 23, 'Significant Influence' has been defined as 'power to participate in the financial and/or operating policy decisions of the investee but is not control over those policies'. In Ind AS 28, the same has been defined as 'power to participate in the financial and operating policy decisions of the investee but is not control or joint control over those policies'. Ind AS 28 defines joint control also.

(ii) For considering share ownership for the purpose of significant influence, potential equity shares of the investee held by investor are not taken into account as per AS 23. As per Ind AS 28, existence and effect of potential voting rights that are currently exercisable or convertible are considered when assessing whether an entity has significant influence or not.

(iii) AS 23 requires application of the equity method only when the entity has subsidiaries and prepares Consolidated Financial Statements. Ind AS 28 requires application of equity method in financial statements other than separate financial statements even if the investor does not have any subsidiary.

(iv) One of the exemptions from applying equity method in the AS 23 is where the associate operates under severe long-term restrictions that significantly impair its ability to transfer funds to the investee. No such exemption is provided in Ind AS 28.

An explanation has been given in AS 23 regarding the term 'near future' used in another exemption from applying equity method, i.e, where the investment is acquired and held exclusively with a view to its subsequent disposal in the near future. This explanation has not been given in the Ind AS 28 as such situations are covered by Ind AS 105, *Non-current Assets Held for Sale and Discontinued Operations*.

(v) Ind AS 28 now permits an entity that has an investment in an associate, a portion of which is held indirectly through venture capital organisations, or a mutual fund, unit trust and similar entities including investment-linked insurance funds, to elect to measure that portion of the investment in the associate at fair value through profit or loss in accordance with Ind AS 109 regardless of whether these entities have significant influence over that portion of the investment.

(vi) Ind AS 28 requires a portion of an investment in an associate or a joint venture to be classified as held for sale if the disposal of that portion of the interest would fulfill the criteria to be classified as held for sale in accordance with Ind AS 105. AS 23 does not specifically deal with this aspect.

(vii) As per AS 23, in separate financial statements, investment in an associate is not accounted for as per the equity method, the same is accounted for in accordance with AS 13, *Accounting for Investments*. As per Ind AS 28, the same is to be accounted for at cost or in accordance with Ind AS 109, *Financial Instruments*.

(viii) AS 23 permits the use of financial statements of the associate drawn upto a date different from the date of financial statements of the investor when it is impracticable to draw the financial statements of the associate upto the date of the financial statements of the investor. There is no limit on the length of difference in the reporting dates of the investor and the associate. As per Ind AS 28, length of difference in the reporting dates of the associate or joint venture should not be more than three months.

(ix) Both AS 23 and Ind AS 28 require that similar accounting policies should be used for preparation of investor's financial statements and in case an associate uses different accounting policies for like transactions, appropriate adjustments shall be made to the accounting policies of the associate. AS 23 provides exemption to this that if it is not possible to make adjustments to the accounting policies of the associate, the fact shall be disclosed along with a brief description of the differences between the accounting policies. Ind AS 28 provides that the entity's financial statements shall be prepared using uniform accounting policies for like transactions and events in similar circumstances unless, in case of an associate, it is impracticable to do so.

(x) As per AS 23, investor's share of losses in the associate is recognised to the extent of carrying amount of investment in the associate. As per Ind AS 28, carrying amount of investment in the associate or joint venture determined using the equity method together with any long term interests which in substance form part of the entity's net investment in the associate or joint venture shall be considered for recognising entity's share of losses in the associate or joint venture.

(xi) With regard to impairment, AS 23 requires that the carrying amount of investment in an associate should be reduced to recognise a decline, other than temporary, in the value of the investment. Ind AS 28 requires that after application of equity method, including recognising the associate's or joint venture's losses, the requirements of Ind AS 109 shall be applied to determine whether it is necessary to recognise any additional impairment loss.