Applying Ind AS

Accounting considerations due to the COVID-19 outbreak

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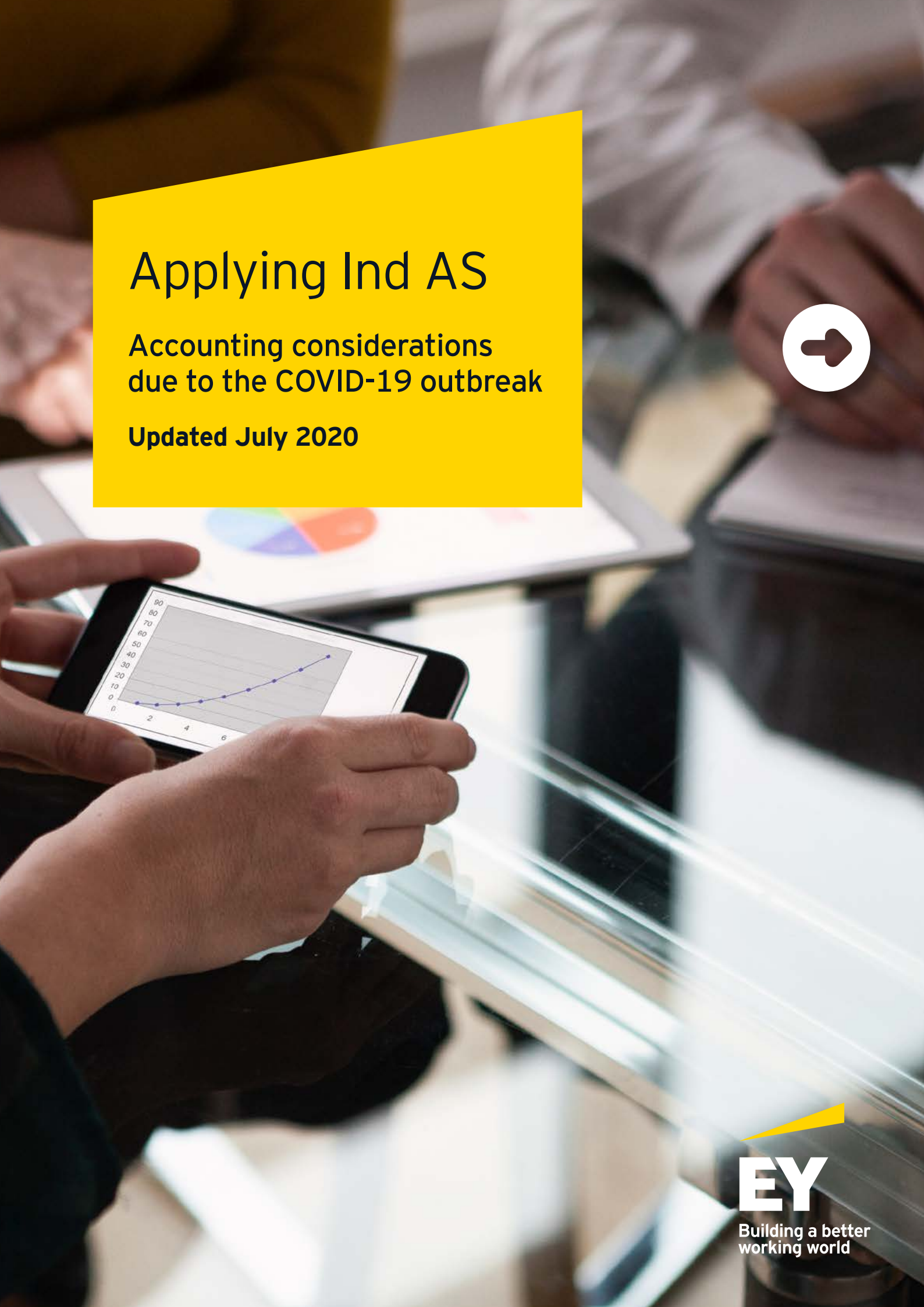

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Foreword

The COVID-19 outbreak has had a significant impact on the business operations of many entities across the globe. While businesses across various parts of the country are resuming their operations gradually as per the directives of the Government, they are still facing challenges due to this sudden change in the macro economic environment. Further, Governments across the globe are also coming up with stimulus packages to give a boost to the economy of respective countries.

Organizations now have some experience of the impacts of the pandemic on their businesses and they are now in a better position to estimate the impacts that may come in future. Accordingly, the estimates made by the management while preparing financial statements for the year ended 31 March 2020 will have to be relooked for the preparation of financial statements for the coming periods. Also entities can leverage from the disclosures made by the entities globally.

In this publication, we have tried to highlight existing accounting principles and impact of proposed amendment to Ind AS 116 which is expected to be issued shortly. It also provides some insights into their application that should be kept in mind when preparing Ind AS Financial Statements considering the impact of COVID-19. We have tried to address most common questions that many entities would be evaluating in the preparation of their financial statements as per Ind AS. This publication was earlier issued in April 2020. In this updated version, we have made certain updates to address some new issues which have evolved since the previous version (refer Appendix 1 for summary of key changes). It also covers impact of the pandemic on financial statements of Top 300 BSE listed companies, based on analysis of financial results for the quarter ended 31 March 2020 which were released till 5 June 2020 (159 out of Top 300 BSE listed companies released their financial results till 5 June 2020). These impacts have been disclosed by way of footnotes in ensuing sections.

It does not attempt to provide an in-depth analysis or conclusive views on the accounting principles. Rather, it aims to highlight key aspects of the existing requirements. Reference should be made to the text of the pronouncements before taking any decisions or actions. The issues discussed are by no means exhaustive and the views expressed herein are more directional and not necessarily conclusive. The applicability of the issues and views expressed in the publication need to be evaluated in light of the facts and circumstances of each entity.

We hope you will find this publication useful in navigating and understanding the impact of coronavirus outbreak on accounting and financial reporting.

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1 Background

The threats posed by the COVID-19 outbreak are not stopping. More countries have imposed travel bans on millions of people and people in more locations are faced with quarantine measures. Businesses are dealing with lost revenue and disrupted supply chains. The disruption to global supply chains due to factory shutdowns has already exposed the vulnerabilities of many organizations. The outbreak has also resulted in significant volatility in the financial and commodities markets worldwide. There are already signs that the virus has significantly impacted the world economy. Various Governments have announced measures to provide both financial and non-financial assistance to the disrupted industry sectors and the affected business organizations.

This publication, therefore, provides a reminder of the existing accounting requirements that should be considered when addressing the financial effects of the coronavirus outbreak in the preparation of Indian Accounting Standard (Ind AS) financial statements. Key presentation and disclosure considerations for annual financial reporting are also covered in this publication. The issues discussed are by no means exhaustive and the views expressed herein are more directional and not necessarily conclusive. The applicability of the issues and views expressed in the publication need to be evaluated in light of the facts and circumstances of each entity. The financial reporting issues, reminders and considerations highlighted in this publication are the following:

- Going concern
- Revenue recognition
- Financial instruments
- Impairment of non-financial assets
- Inventories
- Leases
- Employee benefits
- Provisions and contingent assets
- Government grants
- Income taxes
- Other matters
- Key presentation and disclosures
- Book closure and audit

2 Going concern

Ind AS 1 *Presentation of Financial Statements* requires management, when preparing financial statements, to make an assessment of an entity's ability to continue as a going concern and whether the going concern assumption is appropriate. Furthermore, disclosures are required when the going concern basis is not used or when management is aware, in making their assessment, of material uncertainties related to events or conditions that may cast significant doubt upon the entity's ability to continue as a going concern. Disclosure of significant judgement is also required where the assessment of the existence of a material uncertainty is a significant judgement.

In assessing whether the going concern assumption is appropriate, the standard requires that all available information about the future, which is at least, but not limited to, 12 months from the end of the reporting period, should be taken into account. Refer to section 13 for further discussion on the disclosure of liquidity risk arising out of current vulnerability entities are facing.

Measurement

Management is required to assess the entity's ability to continue as a going concern. When making that assessment, where relevant, management takes into consideration the existing and anticipated effects of the outbreak on the entity's activities in its assessment of the appropriateness of the use of the going concern basis. For example, when an entity has a history of profitable operations and relies on external financing resources, but because of the outbreak, its operations have been suspended before or after the reporting date, management would need to consider a wide range of factors relating to the current adverse situation including, expected impact on liquidity and profitability before it can satisfy itself that the going concern basis is appropriate. Management should consider all available information about the future which was obtained after the reporting date including measures taken by Governments and banks to provide relief to affected entities in their assessment of going concern.

Disclosure

Given the unpredictability of the potential impact of the outbreak, there may be material uncertainties that cast significant doubt on the entity's ability to operate under the going-concern basis. If the entity, nevertheless, prepares the financial statements / financial results under the going-concern assumption, it is required to disclose these material uncertainties in the financial statements in order to make clear to readers that the going-concern assumption used by management is subject to such material uncertainties.

How we see it

The degree of consideration required, the conclusion reached and the required level of disclosure will depend on the facts and circumstances in each case, because not all entities will be affected in the same manner and to the same extent. Significant judgement and continual updates to the assessments up to the date of issuance of the financial statements may be required given the evolving nature of the outbreak and the uncertainties involved.

3 Revenue recognition

The coronavirus outbreak could affect revenue estimates in ongoing customer contracts, including future revenue contracts, in the scope of Ind AS 115 *Revenue from Contracts with Customers* in a multiple way. This could require careful consideration of, for example, variable considerations, collectability, price concessions and stand-alone selling prices. Entities may also need to consider how evolutions in their customary business practices affect their assessments under the revenue model in current situation.

When a contract with a customer includes variable consideration (e.g., discounts, refunds, price concessions, performance bonuses and penalties), an entity is generally required to estimate, at contract inception, the amount of consideration to which it will be entitled in exchange for transferring promised goods or services. The amount of variable consideration an entity can include in the transaction price is constrained to the amount for which it is highly probable that a significant reversal of cumulative revenue recognized will not occur when the uncertainties related to the variability are resolved. The entity may need to update its estimates of variable consideration (including any amounts that are constrained) to reflect an entity's revised expectations about the amount of consideration to which it expects to be entitled, considering uncertainties related to the COVID-19 outbreak.

Further, one of the criteria for a contract to exist is that it must be probable that the entity will be able to collect the consideration to which it will be entitled in exchange for the goods or services that will be transferred to the customer. On account of COVID-19 outbreak, the entity needs to assess its customers' ability to pay to decide whether criteria for revenue contracts are continued to be met or not.

Q1 Considering COVID-19 outbreak, if the entity estimates change in discount to customers for existing open contracts, wherein performance obligation is yet to be performed, will it have any implication on revenue recognition?

Response

Revenue is measured at transaction price which is the amount of consideration to which an entity expects to be entitled in exchange for transferring promised goods or services to a customer. The nature, timing and amount of consideration promised by a customer affect the estimate of the transaction price. When determining the transaction price, an entity should consider the effects of variable consideration (along with constraint on variable consideration).

> Automotive, aviation and oil & gas sectors reported an average decline of 5% to 15% in revenue for the quarter ended 31 March 2020 ("Q4 2020") as compared to quarter ended 31 December 2019

Hence, entities must estimate the discount which it expects to provide to customer as variable consideration and reduce the transaction price accordingly. The change in the transaction price would be allocated to all performance obligations in the contract unless the variable consideration relates only to one or more, but not all, of the performance obligations.

Q2 What will be the revenue recognition implication for the year end if the entity is expecting to receive higher sales returns on account of the COVID-19 outbreak?

Response

Ind AS 115 requires recognition of refund liability if the entity receives consideration from a customer and expects to refund some or all of that consideration to the customer. Accordingly, for the year end, the entity should estimate its refund liability based on its expectation in light of current situation.

Such refund liability is measured at the amount of consideration received (or receivable) for which the entity does not expect to be entitled (i.e., amounts not included in the transaction price). The refund liability (and corresponding change in the transaction price and therefore, the contract liability) shall be updated at the end of each reporting period for changes in circumstances. Entity may also record corresponding asset at cost or net realizable value whichever is lower for right to recover the products if the entity does expect such asset would have a value post return.

Q3 Entities have currently estimated the volume discount to be provided based on expected volume targets to be achieved by customers and reduced the same from the transaction price. Now, if as per revised estimates, volume targets will not be achieved, how would it impact revenue recognition?

Response

Revenue is measured at transaction price which is the amount of consideration to which an entity expects to be entitled in exchange for transferring promised goods or services to a customer. When determining the transaction price, an entity shall consider the effects of variable consideration (along with constraint on variable consideration). An entity that makes such an estimate is also required to update the estimate throughout the term of the contract to depict conditions that exist at each reporting date.

Any reduction in an entity's estimation of customers' ability to achieve volume target will lead to increased transaction price. Such increase in the transaction price would be allocated to all performance obligations in the contract unless the variable consideration relates only to one or more, but not all, of the performance obligations. Additionally, management needs to carefully consider the impact of the above in recoverability of the outstanding collectible from the customer. Further, if the entity were to modify the existing volume targets to enable its customer to receive the incentive then such needs to be evaluated for appropriate accounting and related disclosures.

Q4 Customers' ability to pay consideration is in doubt on account of the COVID-19 outbreak and performance obligation is already satisfied. In such case, entity has deferred the revenue recognition, however, subsequently customer pays. What should be the accounting treatment?

Response

If an entity concludes that collection is not probable and hence, defers the revenue recognition, but a customer subsequently makes the payment, then in such case, it shall recognize the consideration received as revenue on receipt of consideration, since it has already satisfied the performance obligation.

Q5 What are the cut-off considerations for revenue recognition for various INCO terms due to lock down situation caused by the COVID-19 outbreak? For example, when goods are ready for dispatch but could not be dispatched to customers or goods are dispatched but stuck in transit during the lockdown.

Response

An entity shall recognize revenue when goods are transferred, i.e., the customer obtains control of those goods. To determine the point in time at which a customer obtains control of goods, the entity shall consider indicators of the transfer of control, which include, but are not limited to, the following:

a. The entity has a present right to payment for the asset
b. The customer has legal title to the asset
c. The entity has transferred physical possession of the asset
d. The customer has the significant risks and rewards of ownership of the asset
e. The customer has accepted the asset

Entities may be currently following their own cut-off accounting policy for determining timing of revenue recognition for domestic and export sales based on above indicators. However, now entities may need to relook at their policy, particularly for transactions in the month of March, considering the additional risks and delays to be considered with respect to delivery of goods to customer.

Consideration will also have to be given to fact that the transfer of control may not always coincide with transfer of physical possession and none of the indicators mentioned above are a conclusive factor on their own. Hence entities will need to apply significant judgment and evaluate all the relevant factors including the indicators mentioned above to decide on timing of revenue recognition.

Q6 In case the goods were ready for dispatch by the entity but could not be dispatched to customers due to lockdown, can the entities recognize the revenue based on bill-and-hold guidance of Ind AS 115?

Response

In case due to lockdown, goods fail to get dispatched and if there are changes in contractual terms with customer, then evaluation will be required whether such arrangement meets the criteria for bill and hold. A bill and hold arrangement is a contract under which an entity bills a customer for a product but retains physical possession of the product until it is transferred to the customer at a point in time in the future. As per Para B81 of Ind AS 115 for recognizing revenue under bill and hold arrangement, in addition to revenue recognition criteria mentioned in Ind AS 115 for transfer of control at a point in time, all the following criteria must be met:

a. The reason for the bill-and-hold arrangement must be substantive (e.g., the customer has formally requested the arrangement and there is no doubt with respect to customer honoring the contract).
b. The product must be identified separately as belonging to the customer.
c. The product currently must be ready for physical transfer to the customer.
d. The entity should not have used the product or directed it to another customer.

Hence, in addition to revenue recognition criteria mentioned in Ind AS 115, if the entity concludes that all of the criteria mentioned above are met, it shall recognize the revenue.

Further, if an entity recognizes revenue for the sale of a product on a bill-and-hold basis, it should also consider whether it has remaining performance obligations (e.g., for custodial services) to which it is required to allocate a portion of the transaction price.

Q7 **An entity is currently recognizing revenue over a period of time for a long-term contract using the input method. However, after the reporting date, but before financial statements are finalized, it receives intimation from customer for cancellation of the contract due to coronavirus outbreak, will this have any implications on revenue recognition on the reporting date?**

Response

As per Ind AS 10 *Events after the Reporting Period*, events after the reporting period are those events that are favorable and unfavorable and that occur between the end of the reporting period and the date when the financial statements are approved for issue. Events after the reporting period can either be adjusting and non-adjusting events and the distinction between these two events is based on whether the event provides evidence of conditions that existed at the end of the reporting period or not.

In the given case the condition, i.e., customers intimating termination of revenue contract, was not existing as on the reporting date, however, the circumstances which potentially forced the customer to take this decision were in existence at the balance sheet date, it is likely to be considered as an adjusting event on reporting date. Further, if the entity concludes that the impact of termination of revenue contract is material, then the entity to evaluate the disclosure of the nature of the event and its effect on the financial statements.

However, if there are other contracts terminated during this period and such termination is not due to coronavirus outbreak, but other reasons, then evaluation will be required depending on the facts whether it is an adjusting event or not.

Q8 **An entity is currently recognizing revenue over a period of time for a long-term contract using the input method. Under the input method, the entity measures the progress based on the ratio of cost incurred till date viz.-a-viz. the total cost expected to be incurred. Due to coronavirus, the entity incurred certain liquidated damages and shutdown cost as a result of stoppage of work. Whether this cost can be considered for determining the measure of progress?**

Response

Under the input method, revenue is recognized on the basis of the entity's efforts to the satisfaction of a performance obligation relative to the total expected efforts to the satisfaction of that performance obligation.

An entity shall exclude from the input method the effects of any inputs that do not depict the entity's performance in transferring control of goods or services to the customer. Hence in such case, an adjustment to the measure of progress may be required when a cost incurred does not contribute to an entity's progress in satisfying the performance obligation.

In the given case, liquidated damages and shutdown cost do not contribute to an entity's progress in satisfying the performance obligation, but it is incurred on account of coronavirus outbreak as an additional cost which was not estimated earlier. Hence, such cost will not be included in computing the progress.

Q9 **An entity is offering loyalty points to customers along with purchase of merchandise. It is treating the points as separate performance obligation. These points can be redeemed by customers as discounts against future purchase of the merchandise till their expiry.**

However, due to COVID-19, the entity plans to amend the customer loyalty scheme to extend the expiry period and offer higher discount against redemption of points. What will be the accounting implications of the amendment on the scheme?

Response

In case where option to acquire merchandise at discounted price is treated as separate performance obligation, an entity is required to allocate the transaction price to performance

obligations on a relative stand-alone selling price basis. If the stand-alone selling price for the option is not directly observable, an entity shall estimate it. If the option provides a material right to the customer, the customer in effect pays the entity in advance for future goods or services and the entity recognizes revenue allocated to option, when in future goods are transferred against option or when the option expires.

In case there is an amendment in the scheme, the same will be treated as modification of the contract, once it is approved by both the parties. This modification will be treated as part of the existing contract since the remaining goods or services are not distinct and therefore form a part of a single performance obligation that is partially satisfied at the date of modification. Hence the effect that the contract modification has on the transaction price and on the entity's measure of progress towards complete satisfaction of the performance obligation, will be recognized as a reduction of revenue at the date of the contract modification and increase in contract liability (i.e., the adjustment to revenue is made on a cumulative catch-up basis).

Q10 **As per terms of the contract with the customer, the entity was to ensure performance of obligation from either premises of the entity or from customer's premises. Due to lockdown, employees of the entity have started working from home. The entity has communicated its inability to work from customer premises / entity premises. However, the customer neither gave formal acceptance nor raised any objection on the employees of the entity working from home. Can the entity continue to recognize revenue from such contracts?**

Response

A contract is an agreement between two or more parties that creates enforceable rights and obligations. Enforceability of the rights and obligations in a contract is a matter of law. Contracts can be written, oral or implied by an entity's customary business practices. The practices and processes for establishing contracts with customers vary across legal jurisdictions, industries and entities.

Due to lockdown, employees of entity have been forced to work from home which has been duly communicated to customer. In this case, since the entity has already communicated to the customer but the same is neither accepted nor rejected by the customer yet, the entity should evaluate from a legal perspective whether such contract still creates enforceable rights and obligations. For this purpose, entity should consider various clauses of contract including exchange of communications relating to such lockdown situation where employees of the entity are mandated to work from home as per orders of the government authorities.

After such evaluation from a legal perspective, in case the contract still creates enforceable rights and obligations to meet criteria for revenue recognition, then the entity should recognize revenue under Ind AS 115.

How we see it

Entities may need to use significant judgement to determine the effect of uncertainties related to the coronavirus outbreak on its revenue accounting, e.g., estimates of variable consideration (including the constraint) and providing appropriate disclosures. Importantly, the effects are unlikely to be limited to variable consideration. Decisions made in response to the outbreak (such as modifying contracts, transacting with customers during collectability concerns, revising pricing) may also have an effect on the accounting and disclosures for ongoing and future contracts.

4 Financial instruments

While the pandemic continues to spread, the world is undergoing massive adjustments reacting to this outbreak. Though the outcome is unpredictable, and the conditions are still fluid and volatile, these adjustments (or measures) may or may not have a direct impact on the accounting for financial instruments. Ind AS 109 *Financial Instruments* and Ind AS 107 *Financial Instruments: Disclosures* deal with the accounting for financial instruments and the related disclosures.

The occurrence of large-scale business disruptions that potentially give rise to liquidity issues for certain entities might also have consequential impacts on the credit quality of entities along the supply chain. This may also have knock on effects on retail portfolios (consumer and mortgage loans) as many businesses will have to reduce staff numbers resulting in a sharp increase in numbers of unemployed workers. The deterioration in credit quality of loan portfolios, such as that of trade receivables, as a result of the outbreak will have a significant impact on the expected credit loss (ECL) measurement. In responding to these challenges, certain Governments and central banks have introduced or have directed or encouraged commercial banks to introduce, various types of relief measures to corporates, small and medium-sized enterprises or mortgage borrowers.

Governments or regulatory bodies have announced relief measures for extension of payment terms or have asked lenders to allow such relief measures. Further, in many cases, borrowers have approached lenders for renegotiation of terms. Entities should apply the guidance in Ind AS 109 to determine the impact of the change in terms, including those for determining whether the change to the terms result in substantial modification of the contract or not.

Disclosure

Given the inherent level of uncertainty and the sensitivity of judgements and estimates, disclosures of the key assumptions used and judgements made in estimating ECL are particularly important. This is especially the case as they will have likely been materially updated compared to the key assumptions, judgements and estimates applied in the latest annual financial statements. These would include, for example, the values of the key macroeconomic inputs used to analyze multiple economic scenarios and the probability weights of these scenarios, as well as the assumptions used to determine how the different challenges for specific sectors and regions have been taken into account and the effect of any management overlays.

Additionally, entities should provide disclosures to allow users of financial statements to understand the nature of any material reliefs offered to their borrowers, including those enforced by the Governments, and how they have assessed whether they constitute forbearance, whether they result in a substantial

> Banking, financial services and insurance ("BFSI") sector reported INR 16,864 crores provision for credit loss in Q4 2020

modification of the contract, their effect on staging and the impact on the overall ECL. Refer section 13 for discussion on key disclosures regarding risk sensitivities.

Q11 An entity is following simplified approach for impairment assessment of trade receivables and is currently using practical expedient to use provision matrix for determining ECL on these trade receivables. Is there a need for the entity to make any changes to the provision matrix in view of the pandemic?

Response

Entities are allowed to use practical expedients when measuring ECLs, as long as the approach reflects a probability-weighted outcome, the time value of money, and reasonable and supportable information that is available without undue cost or effort about past events, current conditions and forecasts of future economic conditions at the reporting date.

In order to comply with the Ind AS 109 requirements, the entity is required to consider how current and forward- looking information, including impacts of the coronavirus outbreak, might affect their customers' historical default rates. They also need to assess how the information would affect their current expectations and estimates of ECLs. To calibrate the matrix, the entity would adjust its historical credit loss experience with forward-looking information, including impacts of the coronavirus outbreak. The entity should also consider grouping trade receivables based on the industry or geographical location.

Any subsequent information which provides evidence of conditions existing at the reporting date should be adjusted in ECL measurement.

Q12 What elements are impacted on computation of ECL variables? What are the considerations in measuring ECLs and for determining whether significant increase in credit risk (SICR) has occurred?

Response

The following changes are expected in computation of ECL variables:

Probability of default: probability of default might increase due to adverse impact of the outbreak on businesses/ employment of borrowers.

Exposure at default: some of the borrowers may be having unused borrowing facilities and might draw down on those facilities due to liquidity issues or might cease making discretionary over payments. These are expected to result in an increase in exposure at default.

Loss given default: loss given default might increase as there might be change in credit standing of the financial guarantors or in the fair value of assets pledged as collateral due to market volatility.

Entity should consider the following while measuring ECL and determining if SICR has occurred:

- Best efforts should be made to consider all reasonable and supportable information available (about past events, current conditions and forward-looking information (including macro-economic information)).
- Entities may add additional scenarios to their existing scenarios or consider amending one or more of the existing scenarios to incorporate effect of the outbreak.
- It may be appropriate to consider the use of top-down management overlays to embed in the ECL risks not yet fully captured by the models.
- Impact of Government/regulatory support programs should also be considered in assessment of SICR or ECL measurement.
- It would be inappropriate to assert that reasonable and supportable information is unavailable simply because modelling its effects appears difficult or because it would involve a wider than usual range of possible results.
- Entities should, nevertheless, avoid double-counting the effects of various assumptions applied in individual assessment, macroeconomic scenarios and management overlays.
- Due to increase in credit risks, entities might need to closely analyze some of the financial assets which were not posing significant challenges (e.g., security deposits).

Q13 Can an entity perform collective assessment for assessing SICR and measurement of ECL?

Response

Yes. To accelerate the reflection of changes in risk indicators in credit quality not yet detected at an individual level, it may be appropriate to adjust ratings and the probabilities of default (PD) on a collective basis, considering risk characteristics such as the industry or geographical location of the borrowers. For example, a supplier of products or services to the airline industry would likely consider that the PD of its customers has increased irrespective of specific events identified at the level of individual counterparties.

Further, an entity may have already grouped financial instruments based on shared credit risk characteristics. The occurrence of the coronavirus outbreak might change the risk characteristics of certain loans or receivables, because the respective borrowers or customers might engage in businesses, or be based in areas, which have become affected, or are more prone to be affected, by the outbreak. Therefore, entities should consider (re) segmenting (sub)portfolios.

Q14 An entity has given an intragroup loan repayable on demand and expects to recover its full amount. Is the entity required to assess ECL on such loan in view of coronavirus outbreak?

Response

Ind AS 109 does not provide exemption from ECL measurement for intragroup loans repayable on demand. As the contractual term in case of loans repayable on demand is very low, ECL is generally based on the assumption that the loan is demanded at the reporting date, and it would reflect the losses (if any) that would result from this.

The outbreak is likely to have an impact the liquidity position of the group entity and accordingly, it may not be in a position to repay the loan if demanded on the reporting date. In such case, the ECL assessment should consider the expected manner of recovery and recovery period of the intragroup loan. As the entity is expecting to fully recover the loan, the ECL will be limited to the effect of discounting the amount due on the loan at the loan's effective interest rate over the period until the loan is recovered.

Even if full recovery is expected but delayed, ECL measurement should take into account the time value of money.

However, it is pertinent to note that no impact will be there in consolidated financial statement of the group as loan will be eliminated as part of consolidation procedures and any impairment loss recognized in standalone financial statements will need to be reversed.

Q15 An entity had given an unsecured long-term loan to its foreign subsidiary. Due to difficulties being faced by the subsidiary, entity has changed the terms of the loan and its realization is no longer planned or likely in foreseeable future. How should the entity account for exchange differences arising on such loan?

Response

The net investment in a foreign operation includes a monetary item that is receivable from or payable to a foreign operation for which settlement is neither planned nor is likely to occur in the foreseeable future. Unsecured loan, in the current case, will be treated as part of net investment in subsidiary.

Exchange differences arising on translation of this loan, which were currently recognized in profit and loss in both standalone and consolidated financial statements, will now be recognized initially in other comprehensive income until the disposal of the investment in case of consolidated financial statements. However, exchange differences will continue to be recognized in profit and loss in standalone financial statements of the entity even after such loan is treated as net investment in foreign operation.

Q16 An entity has applied for and availed moratorium from payment of interest and principal for a period of three months. During this period, interest on the borrowing continues to accrue as per the original terms. How should the entity account for such moratorium availed?

Response

Payment moratorium results in changes in contractual cash flows (timing and amount (additional interest component) of cash flows) of the financial liability and accordingly will be considered as modification of the contractual terms.

If the entity determines that the modification to contractual terms is substantial, modification should be recorded as extinguishment of financial liability. The carrying value of financial liability should be derecognized and new financial liability should be recognized at its fair value. Any difference between the carrying value and new financial liability will be recognized in profit and loss. Costs and fees incurred on such modification will also be recognized in profit and loss.

If the entity determines that the modification is not substantial, the entity should recalculate the gross carrying amount of the financial liability and recognize a modification gain/loss in profit or loss statement. The gross carrying amount of the financial liability is recalculated as the present value of the modified contractual cash flows that are discounted at the financial liability's original effective interest rate.

Q17 Entities facing financial difficulties may approach lenders for renegotiation, rollover or rescheduling of cash flows. How should this be accounted in the books of the borrower?

Response

As part of renegotiation, rollover or rescheduling of cash flows, parties may also agree to amend other contractual terms of borrowing. Borrower needs to evaluate if the contractual terms are substantially modified and accordingly determine if the modification needs to be accounted as an extinguishment of liability or adjustments are required only in the carrying value of the liability.

Borrower should also perform both quantitative (commonly referred to as the 10% test) and qualitative assessment to determine if modification of terms is substantial. Performing a qualitative assessment may require a high degree of judgement based on the facts and circumstances. Refer question 15 for accounting in such circumstances.

Q18 Is there a need for an entity to consider quoted price as fair value keeping the substantial drop in market price due to COVID-19?

Response

Ind AS 113 *Fair Value Measurement* specifies that fair value measurement (FVM) is a measurement date specific exit price estimate based on assumptions (including those about risks) that market participants would make under current market conditions.

Significant volatility in markets, due to the outbreak, might represent risk assumptions that market participants are making under current conditions. Ind AS 113 specifies that in case of availability of level 1 inputs, the same should be used for fair value measurement. It would not be appropriate to adjust or disregard observable transactions unless those transactions are determined to not be orderly. Ind AS 113 provides a list of factors to consider that may indicate a transaction is not orderly. However, considering the level of operation of current markets, we expect that the fair value of an investment in an active market would continue to be calculated based on quoted prices, even in times of significant market volatility.

Q19 How should subsequent information pertaining to unlisted securities be captured in fair value measurement?

Response

The uncertainties caused by the coronavirus outbreak are expected to result in significant difficulties in determination of fair value measurement particularly in case of instruments where level 1 inputs are not available (e.g. unlisted equity securities). In view of difficulty in obtaining observable inputs pertaining to determination of fair value measurement, management may be relying more on unobservable inputs. Subsequent events may provide evidence of conditions existing at the reporting date (e.g., audited balance sheet of an unlisted entity may become available before financial statements of an entity get approved).

Ind AS 113 specifies that fair value measurement (FVM) is a measurement date specific exit price estimate based on assumptions (including those about risks) that market participants would make under current market conditions. That is, at the measurement date, what assumptions would market participants have made using all available information, including information that may be obtained through due diligence efforts that are usual and customary.

Although events and/or transactions occurring after the measurement date may provide insight into the assumptions used in estimating fair value as of the measurement date (only those that are unobservable), they are only adjusted for in FVM to the extent they provide additional evidence of conditions that existed at the measurement date and these conditions were known, or knowable, by market participants. And accordingly, if such conditions were not in existence at the measurement date, subsequent information should not be treated as adjusting event.

Q20 Does sale of instruments held under hold-to-collect business model due to increase in credit risks of borrowers or to address temporary liquidity crisis represents a change in business model?

Response

A deterioration of the credit quality of the borrower or the issuer of a financial asset, as a result of the outbreak, may result in entities deciding to dispose of their investments classified as hold-to-collect under Ind AS 109.

If the sale is due to an increase in credit risk, this would be consistent with the business model's objective of hold to collect, because the credit quality of financial assets is relevant to the entity's ability to collect contractual cash flows. Selling a financial asset because it no longer meets the credit criteria specified in the entity's documented investment policy is an example of a sale that would be consistent with the business model hold to collect.

Additionally, an increase in the frequency and value of sales in a particular period is not necessarily inconsistent with an objective to hold financial assets in order to collect contractual cash flows, if an entity can explain the reasons for those sales and demonstrate why sales in future will be lower in frequency or value. For example, if, due to a significant decrease in demand for the entity's products or services as a result of the pandemic (e.g., airline tickets or hospitality events) the entity faces a temporary liquidity crisis, the sale of financial assets classified as held-to-collect may not be inconsistent with such business model.

Q21 How will the coronavirus outbreak impact cash flow hedge accounting for a highly probable forecasted transaction?

Response

Due to the coronavirus outbreak, the entity will need to consider whether the transaction is still a highly probable forecasted transaction. This includes whether the volume or amounts involved will be lower than forecasted or whether it is now no longer probable that the forecasted transaction will occur. Depending on conclusions reached, accounting will be as follows:

If forecasted transaction is no longer highly probable, but is still expected to occur

The entity must discontinue hedge accounting prospectively. In this case, the accumulated gain or loss on the hedging instrument that has been recognized in other comprehensive income will remain recognized separately in equity until the forecasted transaction occurs.

If forecasted transaction is no longer expected to occur

The entity must discontinue hedge accounting prospectively. Further, it should immediately reclassify any accumulated gain or loss on the hedging instrument that has been recognized in other comprehensive income to profit or loss.

If forecasted transaction is expected to be delayed

Change in timing of forecasted transaction is a source of hedge ineffectiveness. If the entity decides to retain the derivative and continue to apply the hedge accounting, it should test the effectiveness of the hedge and may the extent the hedge is highly effective.

If effectiveness is being tested through hypothetical derivative, entity may consider redefining the hypothetical derivative to reflect changes in expectations. Further, at the start of each period for which hedge effectiveness is assessed, the entity would need to demonstrate

that hedge relationship will be effective prospectively.

Ineffective portion of the hedge will be recognized in profit and loss. Amount recognized in OCI will be reclassified to profit and loss when forecasted transaction occurs.

Further, the outbreak might also impact management's ability to designate new hedges.

Where forecast transaction is no longer expected to occur, amount reclassified to profit or loss may be presented under other expenses or other income and should not be grouped with revenue or purchases.

Further, the Financial Accounting Standards Board (FASB) staff discussed a question on discontinued cash flow hedges and whether delays in the timing of forecasted transactions related to coronavirus may be considered rare cases caused by extenuating circumstances outside the control or influence of the reporting entity under the guidance in ASC 815-30-40-4. The staff indicated that the exception regarding extenuating circumstances may be applied to coronavirus related delays in the timing of a forecasted transaction. And accordingly, the entity may continue to defer amounts previously recorded in accumulated other comprehensive income (AOCI) until the forecasted transaction affects earnings (provided the forecasted transaction remains probable of occurring). In absence of similar principles under Ind AS and IFRS and similar guidance by International Accounting Standards Board (IASB), the stated FASB guidance may not be applicable to financial statements being prepared under Ind AS or IFRS.

Q22 **An entity has opted for the moratorium in payment of interest and repayment of principal component of a term loan. In view of non-payment of interest and principal repayment during this period, should this be disclosed as continuing default as at reporting date? Further, will this be considered as default for reporting under Companies (Auditor's Report) Order, 2020 ("CARO 2020")?**

Response

Schedule III (Division II and III) to the Companies Act, 2013 requires disclosures of period and amount of continuing default as on the balance sheet date in repayment of borrowings and interest, separately in each case.

Since, moratorium in payment of interest and/ or principal would be agreed mutually by lender or borrower or in some cases may be enforced by regulatory bodies / Government, we are of the view same should not be treated as default in repayment of interest and borrowings.

Further, with respect to reporting under erstwhile CARO 2016, the Institute of Chartered Accountants of India ("ICAI") has issued a publication on *Auditor's Reporting - Key Audit Considerations amid COVID-19* in which it has been clarified that where an entity opted for moratorium and it has made the payment within such extended due dates, it does not constitute a non-compliance and accordingly the same is not required to be reported under CARO. However, the fact that such a moratorium has been granted / approved by banks or financial institutions should be disclosed in CARO. Though the clarification is related to reporting under CARO 2016, we believe the analogy can be drawn for CARO 2020 considering the similar reporting requirements with respect to default in repayment of loans or borrowing to financial institutions and banks under CARO 2020 and CARO 2016.

Q23 **Disruptions resulting from the coronavirus outbreak have impacted compliance of debt covenants of a long-term loan and same has become repayable on demand. How should the entity classify such borrowing in its financial statement?**

Response

The reporting entity should analyze if the breach is material or minor and apply the following guidance:

Breach of minor provision

Guidance note on Division II – Ind AS Schedule III to the Companies Act, 2013 issued by the ICAI provides that in case of minor breach of debt covenants, loan may continue to be classified as non-current unless lenders have recalled the loan before the date of approval of the financial statements on breach of a loan covenant that occurred before the year-end.

Breach of major provision

Ind AS 1 requires classifying long-term loan as current where there is a breach of material provision which makes it payable on demand as on reporting date. However, it should be classified as non-current if the lender agreed not to demand payment, after the reporting period but before the approval of the financial statements for issue. Accordingly, classification would depend whether or not an entity is able to obtain waiver from the lender before approval of financial statements.

Q24 An entity has missed several forecasts due to the effects of the outbreak. How will it affect its ability to designate new hedges in future?

Response

Hedge accounting can be applied only when forecast transactions are highly probable of occurring . The assessment of likelihood of a forecast transaction is not solely based on management's intention but it should also be supported by observable facts and the attendant circumstances. For such an assessment, an entity should also consider the frequency of similar past transactions, among other factors.

However, if an entity has a history of having designated hedges of forecast transactions which subsequently determined to be no longer expected to occur, the entity's ability to predict forecast transactions accurately is called into question when predicting similar forecast transactions. This affects the assessment of whether similar forecast transactions are highly probable. However, Ind AS 109 contains no prescriptive 'tainting' provisions in this area. Therefore, entities are not automatically prohibited from using cash flow hedge accounting if a forecast transaction fails to occur. Instead, whenever such a situation arises the particular facts, circumstances and evidence should be assessed to determine whether doubt has, in fact, been cast on an entity's ongoing hedging strategies.

The FASB staff in a staff question-and-answer document responded that given the unprecedented nature of the pandemic, the FASB staff believes that it would be acceptable for an entity to determine that missed forecasts related to the effects of the COVID-19 pandemic need not be considered when determining whether an entity has exhibited a pattern of missing forecasts that would call into question its ability to accurately predict forecasted transactions and the propriety of using cash flow hedge accounting in the future for similar transactions. The FASB staff further added that this guidance did not contemplate forecasts changing so rapidly as a result of a pandemic.

However, no specific guidance has been issued under Ind AS or IFRS, if missed forecast due to the effects of the outbreak can be ignored when determining an entity's ability to predict forecast transactions accurately. In absence of specific guidance under Ind AS or IFRS, as present situation is not stable and is fluid, so entities should take additional care in assessing whether a forecast transaction meets the test of being highly probable. Entities will have to apply additional judgement in determining if missed forecast due to the effects of the outbreak can be ignored when determining an entity's ability to predict forecast transactions accurately.

How we see it

The assessment of the impact of the coronavirus outbreak on ECL will require significant judgement, especially as it is not directly comparable with any recent similar events. Entities will have to update their macroeconomic scenarios and consider the use of top-down 'management overlays' to embed in the ECL risks not yet fully captured by their models. Given the level of uncertainty and the sensitivity of judgements and estimates, disclosures of the key assumptions used and judgements made in estimating ECL, as well as the impact of any relief measures, is going to be critical.

5 Impairment of non-financial assets

An asset is impaired when an entity is not able to recover its carrying value, either by using it or selling it. An entity estimates the recoverable amount of the asset for impairment testing. Recoverable amount is the higher of the fair value less costs of disposal (FVLCD) and the value in use (VIU). Value in use is defined as the present value of the future cash flows expected to be derived from an asset or cash generating unit. The calculation of an asset's value in use incorporates an estimate of expected future cash flows and expectations about possible variations of such cash flows.

Ind AS 36 *Impairment of Assets* requires an entity to assess, at the end of each reporting period, whether there is any impairment for an entity's non-financial assets. For goodwill and intangible assets with indefinite useful lives, Ind AS 36 requires an annual impairment test and when indicators of impairment exist. For other classes of assets within the scope of the standard, an entity is required to assess at each reporting date whether there are any indications of impairment. The impairment test only has to be carried out if there are such indications.

In cases where entities are receiving government grants in relation to the pandemic and these cash flows are part of the recoverable amount, entities should carefully consider the conditions of any government grant in order to assess whether the inclusion of such amounts in the impairment test is based on reasonable and supportable assumptions that represent management's best estimate of the range of economic conditions that will exist over the remaining useful life of the asset or cash generating units.

Events after the reporting period and information received after the reporting period should be considered in the impairment indicator assessment only if they provide additional evidence of conditions that existed at the end of the reporting period. Judgement of all facts and circumstances is required to make this assessment.

Disclosure

The more the current environment is uncertain, the more important it is for the entity to provide detailed disclosure of the assumptions taken, the evidence they are based on and the impact of a change in the key assumptions (sensitivity analysis). Given the inherent level of uncertainty and the sensitivity of judgements and estimates, disclosures of the key assumptions used and judgements made in estimating recoverable amount will be particularly important. This is especially the case as they will have likely been materially updated compared to the key assumptions, judgements and estimates applied in the latest annual financial statements. These would include, for example, the values of the key assumptions and the probability weights of multiple scenarios when using an expected outcome approach.

> Impairment provisions of INR 2,185 crores have been provided by nine companies in Q4 2020

Q25 Can impairment loss recognized in current period may be subsequently reversed when economic outlook improves in subsequent periods?

Response

If there is any indication that an impairment loss recognized in prior periods for an asset / cash generating unit (CGU) other than goodwill may no longer exist or may have decreased, the entity shall estimate the recoverable amount of that asset / CGU and increase its carrying value to its recoverable amount. However, the revised carrying amount of an asset shall not exceed the carrying amount that would have been determined (net of amortization or depreciation) had no impairment loss been recognized for the asset in prior years. A reversal of an impairment loss for a CGU shall be allocated to the assets of the unit, except for goodwill, pro rata with the carrying amounts of those assets. In allocating a reversal of an impairment loss for a CGU, the carrying amount of an asset shall not be increased above the lower of i) its recoverable amount (if determinable); and (ii) the carrying amount that would have been determined (net of amortization or depreciation) had no impairment loss been recognized for the asset in prior periods.

Once an impairment loss has been recognized for goodwill, Ind AS 36 prohibits its reversal in a subsequent period. The standard justifies this on the grounds that any reversal 'is likely to be an increase in internally generated goodwill, rather than a reversal of the impairment loss recognized for the acquired goodwill', and Ind AS 38 *Intangible Assets* prohibits the recognition of internally generated goodwill.

Q26 Should coronavirus outbreak be treated as a trigger for impairment?

Response

An entity is required to assess at the reporting date whether there are any indicators of impairment. With the recent developments of the coronavirus outbreak, there are both external and internal sources of information, such as the fall of stock and commodity prices, decrease of market interest rates, manufacturing plant shutdowns, shop closures, reduced demand and selling prices for goods and services, indicating that an asset may be impaired.

However, outbreak may have impacted different entities differently (such as, entities engaged in provision of essential goods/ services) and triggers should be analyzed considering facts and circumstances of each entity.

Q27 Due to the coronavirus outbreak, there were indicators that an asset might be impaired. Management performed the impairment assessment but the same did not result in recognition of impairment loss. Are there any other considerations that management should be careful about in such case?

Response

Ind AS 36 requires that if there is an indication that an asset may be impaired, this may indicate that the remaining useful life, the depreciation / amortization method or the residual value for the asset needs to be reviewed and adjusted in accordance with the standard applicable to the asset, even if no impairment loss is recognized for the asset.

Accordingly, management needs to mandatorily review accounting estimates towards useful life, depreciation / amortization method and residual value, even if no impairment loss is recognized. It is pertinent to note that such review is required even if impairment loss is recognized.

Further, impairment loss recognized will also affect temporary differences as this will generally not impact tax base of related assets. Deferred tax in respect of any deductible temporary difference should be recognized only to the extent that it is probable that taxable profit will be available against which the underlying deductible temporary differences can be utilized.

Q28 What considerations should be taken into account in projecting cash flows where recoverable amount is estimated based on value in use?

Response

Forecasted cash flows should reflect the management's best estimate at the end of the reporting period of the economic conditions that will exist over the remaining useful life of the asset. With the current uncertain situation, significant challenges are expected to prepare the forecast of or budgets for future cash flows and there will probably be a wider range of reasonably possible cash flow projections. In these circumstances, an expected cash- flow approach based on probability-weighted scenarios may be more appropriate to reflect the current uncertainty than a single best estimate when estimating value in use. The potential impact of measures taken to control the spread of the virus could be included as additional scenarios in such an approach.

Under the expected cash flow approach, the uncertainty about future cash flows is reflected in the different probability-weighted cash flow projections used, rather than in the discount rate. The expected cash flow approach inherently requires a more explicit consideration of the wider than normal range of possible future outcomes.

Ind AS 36 requires that cash flow projections can only cover a maximum period of five years, unless a longer period can be justified. If the management is confident that its projections are reliable and can demonstrate this from past experience, it may use a longer period. However, considering current uncertainties, management may find it difficult to justify and demonstrate that projections beyond a period of five years are reliable. This is because past experiences may generally no longer hold good.

Since the remaining useful life for many assets, such as goodwill (indefinite life), is long term, entities should consider not just the short-term effects, but especially the long-term effects.

Q29 How should an entity determine appropriate discounting rate to be used for impairment testing?

Response

The discount rate to be used is a pre-tax rate that reflects current market assessments of the time value of money and the risks specific to the asset for which the future cash flow estimates have not been adjusted. This means that the discount rate to be applied should be an estimate of the rate that the market would expect on an equally risky investment. The outbreak is expected to have a significant impact on the risk-free rate and on specific risk premiums used in determining the appropriate discount rate to discount future cash flows.

As a starting point, an entity may take current risk-free market rate of interest as of the date when assessment is being performed. The risk-free rate is generally based on the yield on Government bonds that have the same or similar duration as cash flows of the asset or cash generating unit. Interest rate so arrived may be adjusted to reflect specific risks associated with the projected cash flows (such as country, currency, price and cash flow risks). Though risk-free rates have decreased, the same may not necessarily result in lowering of discounting rate. This is because uncertainty may result in increase in risk premiums.

To avoid double counting, the discount rate should not reflect risks for which future cash flow estimates have been adjusted.

Q30 Entity is considering restructuring on account of disruption caused by coronavirus outbreak, which will improve cash flows from assets subject to impairment assessment. How should an entity give effect to such restructuring when calculating recoverable amount?

Response

Ind AS 36 requires that estimates of future cash flows shall not include estimated future cash inflows or outflows that are expected to arise from a future restructuring to which an entity is not yet committed. Estimates of future cash inflows and cash outflows for the purpose of determining value in use reflect cost savings and other benefits from the restructuring if the entity is committed to such restructuring and related provision are recognized under Ind AS 37.

However, restructurings should be included in determination of fair value less cost of disposal if a market participant would reasonably expect such restructurings to take place.

Considering that future restructuring is not allowed to be factored in, impairment losses recognized may need to be reversed once the expenditure has been incurred and the restructuring is completed.

Q31 As a containment measure, the Government has imposed lockdown and manufacturing plant has been shut down? Should an entity consider costs required to restart the plant when determining recoverable amount?

Response

Ind AS 36 requires that cash flow projections should include cash outflows that are necessarily incurred to generate the cash inflows from continuing use of the asset including cash outflows necessary to prepare the asset for use. As an entity is necessarily required to restart the plant to generate cash inflows, restart costs should be treated as cash outflows necessary to prepare the asset for use and factored in cash flow projections for determining value in use.

Further, this should also be captured in determination of fair value less cost of disposal as market participants would reasonably expect such cash outflows to be incurred.

Q32 After reporting date an entity has done restructuring causing a change in CGU and expected cash flows, how should it incorporate this in impairment assessment on reporting date?

Response

Events after the reporting period and information received after the end of the reporting period should be considered in the impairment assessment only if changes in assumptions provide additional evidence of conditions that existed at the end of the reporting period. Since change in composition of CGU has happened after reporting date, it should not be considered for impairment assessment as at reporting date.

Q33 How will the coronavirus pandemic impact ongoing capex projects and intangible assets with indefinite useful life?

Response

An entity may have suspended ongoing capex projects due to liquidity/manpower / restrictions imposed by local authorities. Further, the project may no longer remain viable owing the current economic outlook. It may affect the planned use and economics of the project. An entity should consider the conditions existing as at reporting date to determine if indicators of impairment are present and recognize appropriate impairment losses, if any.

Ind AS 38 prohibits amortization of an intangible asset with an indefinite useful life. Instead, Ind AS 36 requires such an asset to be tested for impairment annually and whenever there is an indication that the intangible asset may be impaired. An entity is required to review and validate at the end of each reporting period and its decision to classify the useful life of an intangible asset is indefinite. Due to the coronavirus outbreak, management may be considering any restructuring and may lead to the useful life of some intangible assets becoming finite (for example, the management may be considering discontinuing a particular line of products causing the associated trademark to have a finite life). In case of change in useful life from indefinite to finite, an entity should start amortization of the asset treating such change as a change in accounting estimate.

Q34 **Is impairment assessment required even for right-of-use (ROU) assets? What are some specific considerations when performing such assessments?**

Response

Ind AS 36 also applies to ROU assets and accordingly, ROU or any CGU to which it belongs will be subject to impairment assessment when there are indicators of impairment.

In case of lease arrangements, in most cases a CGU would be disposed of together with the associated lease arrangements. Fair value less cost of disposal for the CGU would consider the associated lease arrangements and therefore the need to make contractual lease payments. This would require deducting the carrying amount of the lease liabilities when determining the carrying amount of the CGU.

Lease payments reflected in the lease liability recorded in balance sheet will have to be excluded from the value in use calculation. If the carrying amount of the lease liabilities is deducted to arrive at the carrying amount of the CGU, the same carrying amount of the lease liabilities would need to be deducted from the value in use. Cash forecasts for value in use calculation should capture lease payments not recognized in financial statements (such as, variable lease payment not dependent on an index or rate).

How we see it

As the crisis evolves and the conditions are unpredictable, at this stage, the management is required to exercise significant judgement to assert reasonable assumptions which reflect conditions existing at the reporting date for impairment testing. We expect that in the current situation, majority of these assumptions are subject to significant uncertainties. As such, entities should consider providing detailed disclosures on assumptions and sensitivities.

6 Inventories

Inventories are valued at lower of cost or net realizable value (NRV). Net realizable value is the estimated selling price in the ordinary course of business less the estimated cost of completion and the estimated cost necessary to make the sale. The economic disruption caused by coronavirus will pose challenges with respect to determination of NRV at the reporting date. Further, due to disrupted production in the last quarter of a financial year, determination of cost of inventories with respect to allocation of excess overheads also needs to be assessed.

Q35 How should NRV of inventory be determined in the current market conditions?

Response

Estimates of net realizable value must be based on the most reliable evidence available and consider fluctuations of price after the end of the reporting period if this is evidence of conditions existing at the end of the reporting period. So, for the entity following March as year-end, coronavirus outbreak is the condition existing on the reporting date. Price realized of inventory post reporting period may provide evidence of the NRV of inventories at the end of the period. NRV determination should be normally done on an item to item basis unless it is not practically possible to evaluate separately.

It is notable that if finished goods and work-in-progress need to be written down below cost due to significant deterioration in market conditions, the entity needs to assess if the raw material and other supplies held for use in the production of finished goods and work-in-progress also need to be written down below cost.

> Inventory write-down of INR 5,555 crores has been provided by oil & gas companies due to COVID-19 and other changing market variables in Q4 2020

Q36 How should an entity value the inventory at reporting date which was produced for a customer contract which is cancelled before reporting date due to coronavirus outbreak?

Response

Estimates of NRV should take into consideration purpose for which the inventory is held. Therefore, inventory held for a particular contract has its net realizable value based on the contract price, and any excess inventory held would be based on general selling prices.

In case the contract for which inventory is held by an entity stands cancelled, the entity needs to evaluate its ability to sell such inventory in the market and the corresponding

costs associated with it. If the entity will not be able to sell the inventory for any reason, the entity needs to assess the impairment loss in inventory as on reporting date. In other cases, the entity can estimate the NRV based on expected selling price and costs to be incurred.

Q37 **As a containment measure, Governments have enforced lockdowns in several territories and production of non-essential goods were stopped. How should an entity treat fixed overheads incurred during this period?**

Response

Ind AS 2 *Inventories* requires fixed production overheads to be included in the cost of inventory based on normal production capacity. The amount of fixed overhead allocated to each unit of production is not increased because of low production or idle plant. Reduced production might affect the extent to which overheads can be included in the cost of inventory. Unallocated overheads should be recognized as an expense during the period in which they are incurred.

Q38 **Lockdowns in several territories and production of non-essential goods has been stopped by the Government resulting in the entity facing sizeable shut down costs for production plants and may also have suffered loss of Work-in-Progress ("WIP") inventory. How should an entity treat such cost?**

Response

The incremental cost and wastages incurred as a consequence of the coronavirus outbreak shall be treated as abnormal amount of wasted material, labour and production cost. Ind AS 2 excludes such abnormal cost from capitalization as part of the inventories. Accordingly, such costs shall be recognized as expenses in the profit and loss during the period in which they are incurred.

How we see it

Entities may need to write down the inventory due to losses, obsolescence and non-movement in the near short to medium term. If the finished goods need to be written down below cost, the entity also needs to assess the realizable value of its raw material and other supplies held for use in the production. Also, there could be additional aspects for entity to consider such as how to value stock in transit, inventory produced in response to customer contracts which is now cancelled, and how to perform physical verification of inventory at year-end.

7 Leases

A lessor and lessee might renegotiate the terms of the lease or any concessions in lease payments may be received by a lessee because of the coronavirus outbreak. When any concessions in lease payments are received by a lessee, it is necessary to evaluate whether Ind AS 116 applies to such lease concessions.

In some jurisdictions, local authorities have implemented policies to provide subsidies to lessees and others in order to support the local economy and these payments are accounted for under Ind AS 20 *Accounting for Government Grants* and Disclosures of Government Assistance. Refer to section 10 for a discussion on the related accounting considerations.

Many lessees may face financial difficulties due to government-mandated closure of businesses. This may cause a significant deterioration in collectability of lease payments from certain lessees.

Unlike other standards such as Ind AS 115, Ind AS 116 does not refer to collectability to determine whether (and when) lease income should be recognized. We believe that a lessor may continue to recognize operating lease income even when collectability is not probable. However, other approaches may also be appropriate when there is significant doubt about collectability. Therefore, there could be diversity in practice and it is important to consider the view from the local regulator. Regardless of the approach followed, Ind AS 109's guidance on credit losses continues to be applicable to recognized lease receivables.

Under Ind AS 116, a lessor of a finance lease is required to apply the impairment requirements in Ind AS 109 to the net investment in the lease.

Q39 How should entities account for lease concessions so received, either in terms of reduction of lease rent or in terms of reduction of scope, as lessee?

Response

When Ind AS 116 applies to such lease concessions, the lessee and lessor need to evaluate if there is a lease modification by considering the original terms and conditions of the lease. Under Ind AS 116, a lease modification is a change in the scope of a lease, or the consideration for a lease, that was not part of the original terms and conditions of the lease.

If the lease concessions so received is not contemplated under the terms and conditions of the original lease:

For a lease modification, at the effective date of the lease modification, a lessee is required to allocate the

> ICAI has issued Exposure Draft on COVID-19-Related Rent Concessions (Proposed amendment to Ind AS 116) corresponding to amendments in IFRS 16 issued by the International Accounting Standards Board

consideration in the modified contract, determine the lease term of the modified lease and remeasure the lease liability by discounting revised lease payments using a revised discount rate with a corresponding adjustment to right-of-use asset. If the modification decreases the scope of the lease, the lessee accounts for the remeasurement of the lease liability by decreasing the carrying amount of the right-of-use asset to reflect the partial or full termination of the lease and recognizes in profit or loss any gain or loss relating to the partial or full termination. The lessee should even consider if this event is an indicator which triggers an impairment test for its right-of-use asset.

Further, the IASB has issued an amendment to IFRS 16 to provide relief to lessees from applying IFRS 16 guidance on lease modification accounting for rent concessions. An entity making this election needs to account for any change in lease payments resulting from the COVID-19 rent concession in the same way it would account for the change applying IFRS 16, if the change was not a lease modification (refer Q48 for further discussion). This exemption can be availed for rent concessions occurring as a direct consequence of the COVID-19 pandemic and only if all of the following conditions are met:

a. The change in lease payments results in revised consideration for the lease that is substantially the same as, or less than, the consideration for the lease immediately preceding the change

b. Any reduction in lease payments affects only payments originally due on or before 30 June 2021 (for example, a rent concession would meet this condition if it results in reduced lease payments on or before 30 June 2021 and increased lease payments that extend beyond 30 June 2021)

c. There is no substantive change to other terms and conditions of the lease

In line with above amendments, the ICAI also has issued exposure draft on proposed amendments to Ind AS 116 and same is proposed to be effective for reporting periods beginning on or after 1 April 2020 with earlier application permitted ("proposed amendments").

If the lease concessions so received is contemplated under the terms and conditions of the original lease:

In such cases, accounting shall depend on the specific fact pattern of the case. If the lease concessions so received is a variable lease payment not indexed to a rate that varies because of changes in the fact and circumstances occurring after the commencement date of the lease, it may be appropriate to treat the payment as a negative variable consideration to be recognized in profit or loss. Further, the lessee should even consider if this event is an indicator which triggers an impairment test for its right-of-use asset.

Q40 An entity is preparing its quarterly results for 30 June 2020. If proposed amendment referred above (Q39) is notified before finalization of quarterly results but after 30 June 2020, can entity apply this amendment in its quarterly results?

Response

As per the Exposure Draft, the proposed amendments are effective for the reporting periods beginning on or after 1 April 2020 with early application permitted. If amendment is notified before the finalization of quarterly results and effective for reporting period covered by the quarterly results, an entity can avail the exemption based on the transition date mentioned in the amendment while preparing its financial statements for the quarter ended 30 June 2020.

Q41 What should be the discount rate used to account for lease modification?

Response

The modification of the lease requires the remeasurement of the lease liability using a revised discount rate as on the date of modification. Given that the interest rate implicit in the lease is generally not readily determinable by the lessee, it is necessary for the lessee to determine a revised incremental borrowing rate as on effective date of modification. The coronavirus outbreak has exacerbated market volatility and central banks in many jurisdictions are cutting interest rates. Assessing a revised incremental borrowing rate may also require judgement in these circumstances.

Q42 How should an entity account for lease concessions as lessor?

Response

If the lessor has accounted for the lease as an operating lease, a lessor recognizes lease payments from operating lease as income on either straight-line basis or another systematic basis. If such a lease is modified on account of the lease concessions being offered by a lessor due to the coronavirus outbreak, the same shall be accounted as new lease from the effective date of modification, considering any prepaid or accrued lease payments relating to the original lease as part of lease payments for the new lease.

If the lessor has accounted for the lease as finance lease, they would have recognized such a lease as on commencement date at an amount equal to net investment in the lease. In case of modification of such lease, which is not accounted for as separate lease, the lessor needs to reassess the finance lease receivable recognized with a corresponding impact in profit and loss.

Q43 When lease modifications should be recorded by lessor and lessee?

Response

A lease modification is a change in the scope of a lease, or the consideration for a lease, that was not part of the original terms and conditions of the lease. For the lease modification that is not accounted as separate lease, lease modification should be recorded, by both lessor and lessee, at the effective date of the modification of lease. For the purpose, the effective date of the modification is defined as the date when both parties agree to the lease modification.

Accordingly, if the lease modification is effected by parties post reporting date, the same shall not be accounted for in the financial statements for the year ended 31 March 2020. However, if the modification is material enough, the same should be disclosed as event after the balance sheet date (Refer section 13 for details on disclosures).

Q44 Given the decrease in interest rates, should the entity change discount rates used for discounting lease payments of existing leases?

Response

Even though rates may have come down because of economic disruption caused by the coronavirus outbreak, a lessee should not change discount rates for balance lease payments under existing leases for which there is no lease modification / reassessment.

Q45 If the entity makes an assessment whereby ROU asset is impaired due to disruption caused by the coronavirus outbreak, does the entity need to do impairment testing for leasehold improvements made for such ROU?

Response

Where leasehold improvements generate cash flows that are individually identifiable and independent of an ROU asset, impairment of ROU assets is not necessarily an impairment trigger for leasehold improvements and it has to be assessed independently if any triggers of impairment exist for leasehold improvements. However, where leasehold improvements do not generate independent cash flows, they will be generally part of CGU to which an ROU asset belongs and will be tested for impairment along with the ROU asset.

Q46 If the entity terminates the lease which is entered but not commenced due to disruptions caused by the coronavirus outbreak, how should the initial direct cost incurred for such lease be accounted for?

Response

Ind AS 116 defines initial direct cost as incremental cost of obtaining a lease that would not have been incurred if the lease had not been obtained. if further requires lessees to include their initial direct cost in their initial measurement of the ROU asset. Accordingly, the entity would have capitalized such initial direct costs for the leases which are entered into. If the entity terminates the leases which are yet to commence, the initial direct costs so capitalized with respect to such lease should be charged to profit and loss.

Q47 **An entity had obtained premises on lease for a period of five years commencing 1 April 2019 at a monthly lease payment of INR 4,000. Entity has received rent concession as a direct consequence of COVID-19 pandemic. How would the proposed amendment be applicable in different scenarios?**

Response

(Note: The response below is based on exposure draft on proposed amendments to Ind AS 116 and needs to be relooked if final amendments are not in line with current draft.)

An entity, being a lessee, is permitted to avail exemption from applying lease modification guidance in Ind AS 116. The practical expedient applies only to rent concessions occurring as a direct consequence of the COVID-19 pandemic and only if all of the following conditions are met:

a. The change in lease payments results in revised consideration for the lease that is substantially the same as, or less than, the consideration for the lease immediately preceding the change

b. Any reduction in lease payments affects only payments originally due on or before 30 June 2021 (for example, a rent concession would meet this condition if it results in reduced lease payments on or before 30 June 2021 and increased lease payments that extend beyond 30 June 2021)

c. There is no substantive change to other terms and conditions of the lease.

Sr. no.	Scenario	Response
1	Rent is reduced to INR 3,000 for May 2020 -July 2020 and increased by INR 1,000 from original rent for August 2020 to October 2020, i.e., will pay INR 5,000 for these three months. Apart from this, there is no change in any term or conditions of the lease	Yes. The practical expedient can be availed as all three conditions are met
2	Rent is reduced for period before June 2021 but increased thereafter to compensate for time value of money. Apart from this, there is no change in any term or conditions of the lease	Yes. If the nominal cash flows have increased to compensate for the time value of money, it would appear appropriate for entities to assess that consideration for lease is substantially the same. Other increases in consideration, such as penalties that are included in the deferral, would cause this criterion to not be satisfied
3	Rent is reduced to INR 3,000 for May 2020 -July 2021	No. Reduction in lease payment affects lease payments originally due after June 2021. In this regard, it may be noted that, the lease rentals are to be considered in its entirety. If a rent concession resulted in reduced lease payments beyond June 2021, the entire rent concession would fail this criterion and the practical expedient would be unavailable. It is not acceptable that rent concessions are apportioned such that that one portion satisfies the criterion (i.e. May 2020 –June 2021) and remaining portion, i.e., July 2021 does not satisfy the criterion

Sr. no.	Scenario	Response
4	Lease payment is reduced to INR 3,000 for May 2020 -July 2020 and increased by INR 4,000 for August 2021-October 2021	No. Change in lease payments results in consideration for the lease being significantly higher than consideration preceding such change and increase does not appear to represent time value of money
5	Lessor agrees to reduce the monthly lease payment provided leased space is reduced from 8,000 sq. ft to 5,000 sq. ft.	No. Change results in substantive change to other terms of the lease (scope is being decreased)
6.	Lessor agrees for rent holiday for May 2020 -July 2020. However, at the end of the lease term, it got extended for another 3 months with substantially equivalent payments. Apart from this, there is no change in any term or conditions of the lease.	Yes. Three months rental holiday before 30 June 2021, followed by three additional months of substantially equivalent payment at the end of the lease would not constitute a substantive change to other terms and conditions of the lease. A simple concession that essentially replaces the period of the rent concession with an equivalent period at the end of the lease and with substantially equivalent payments can be considered not to be a substantive change to the lease but, instead, simply a payment concession. However, if additional changes were made, this would not be the case.

Q48 **In case an entity has evaluated that reduction in lease payments is occurring as a direct consequence of the COVID-19 pandemic and all other conditions for availing practical expedient in proposed amendments are satisfied (refer Q39 for conditions). How should it account for concessions in the following cases?**

a. Lessor forgives the lease rentals

b. Lessor defers the lease rentals

Response

(Note: The response below is based on exposure draft on proposed amendments to Ind AS 116 and needs to be relooked if final amendments are not in line with current draft.)

The amendment to Ind AS 116 does not provide explicit guidance about how a lessee accounts for a rent concession when applying the practical expedient. It states that a lessee making the election accounts for any change in lease payments resulting from the COVID-19 related rent concession the same way it would account for the change under Ind AS 116, if the change were not a lease modification.

We believe there are several potential approaches for accounting for a rent concession which is not accounted for as a lease modification, including:

- Accounting for a concession in the form of forgiveness or deferral of lease payments, as a negative variable lease payment (Approach 1)
- Accounting for a concession in the form of forgiveness or deferral of lease payments, as a resolution of a contingency that fixes previously variable lease payments (Approach 2)
- Accounting for a concession in the form of a deferral of payments as if the lease is unchanged (Approach 3)

Approach 1

When a lessor grants a concession that contractually releases a lessee from certain lease payments or defers lease payments, we believe a lessee may account for the concession as a negative variable lease payment. In this case, the lessee would remeasure the remaining

consideration in the contract and, if the contract contains multiple lease and non-lease components, reallocate the consideration to the lease and non-lease components (using unchanged allocation percentages). The lessee would also not update the discount rate used to measure the lease liability. In this case, the lessee would recognize the allocated portion of the forgiven payments as a negative variable lease expense in the period when changes in facts and circumstances on which the variable lease payments are based occur. This approach is similar to that used by the lessor to recognize variable lease income.

Approach 2

Under this approach, we believe that a lessee may account for a rent concession in the same manner as it would account for a resolution of a contingency that fixes previously variable lease payments. In this case, the lessee would remeasure the remaining consideration in the contract and, if the contract contains multiple lease and non-lease components, reallocate the consideration to the lease and non-lease components (using unchanged allocation percentages). The lessee would also not update the discount rate used to measure the lease liability. Therefore, the lessee would remeasure its lease liability, using the remeasured consideration (e.g., reflecting the lease payment reduction or lease payment deferral provided by the lessor), with a corresponding adjustment to the right-of-use asset.

Approach 3

When a lessor permits a lessee to defer a lease payment, we believe the lessee may account for the concession by continuing to account for the lease liability and right-of-use asset using the rights and obligations of the existing lease and recognizing a separate lease payable (that generally does not accrue interest) in the period that the allocated lease cash payment is due. In this case, the lessee would reduce the lease payable when it makes the lease payment at the revised payment date.

This approach of recording a lease payable for the future payment would allow the lease liability to be accreted using the original incremental borrowing rate and would result in a lease liability balance of zero at the end of the lease term (i.e., the lessee would not need to revisit the accretion of its lease liability based on the revised timing of payments). In many cases, this will allow a lessee to use its existing systems to account for the lease liability using the existing payment schedule and discount rate.

Q49 **B ("Lessee") entered into an agreement with a shopping mall owner A ("Lessor") for space in the mall. The lease term was 3 years and commenced from 1 April 2019. Lease payment fixed by the lessor was INR 10,000 p.m. to be paid on the 1st day of each month. On 31 March 2020, based on government directions, lessee closed its shop temporarily due to the outbreak. Consequently, lessor provides 3 month rent concession to lessee starting from May 2020. Lessee has evaluated that such reduction in lease payments is occurring as a direct consequence of the COVID-19 pandemic and all other conditions for availing practical expedient in proposed amendments are satisfied (refer Q39 for conditions). How should B account for such concession in case Lessor A forgives the lease rentals as per the approaches discussed in Q48? For simplicity, the discount rate is assumed to be 0%.**

Response

(Note: The response below is based on exposure draft on proposed amendments to Ind AS 116 and needs to be relooked if final amendments are not in line with current draft.)

Approach 1:

Account for the forgiveness as a negative variable lease payment

The point of recognition is in the period in which the event that triggers the payment occurs, i.e., 1 May 2020.

Lessee B accounts for the reduction in future lease payments by derecognizing the part of the lease liability which has been forgiven and recognizing the adjustment in profit or loss.

Hence, following entry will be passed:

Particulars	Dr. / Cr.	Amount
Lease liability	Dr.	30,000
Profit or Loss	Cr.	30,000

Depreciation of the right-of-use asset continues over the remaining lease term.

Approach 2:

The point of recognition is in the period in which the event that triggers the payment occurs i.e. 1 May 2020. On 1 May 2020, Lessee B treats the concession as an event or condition which resolves uncertainty or conditionality on the previous lease payments. Lessee accounts for the reduction in future lease payments by derecognizing the part of the lease liability which has been forgiven and adjusting the right-of-use asset.

Particulars	Dr. / Cr.	Amount
Lease liability	Dr.	30,000
Right -of -use asset	Cr.	30,000

Depreciation of the revised right-of-use asset continues over the remaining lease term.

Note that if the fact pattern were changed such that the lessee is entitled to a reduction in lease payments for June and July on a month-by-month basis (i.e., if conditions related to COVID-19 continue to be present the monthly lease liability is contractually forgiven), the reduction in the lease obligation would also be recognized monthly. The corresponding credit to profit and loss or the right-of-use asset would depend on whether Approach 1 or Approach 2 is taken.

The lease liability will be reduced by the contractual amount, i.e., INR 10,000 in profit and loss or by crediting right-of-use asset.

Accounting in each month, i.e., from May 2020 - July 2020

Under Approach 1

Particulars	Dr. / Cr.	Amount
Lease liability	Dr.	10,000
Profit or Loss	Cr.	10,000

Under Approach 2

Particulars	Dr. / Cr.	Amount
Lease liability	Dr.	10,000
Profit or Loss	Cr.	10,000

Q50 **B ("Lessee") entered into an agreement with a shopping mall owner A ("Lessor") for space in the mall. Under the terms of the lease, B makes fixed lease payments to A of INR 60,000 semi-annually in arrears. The non-cancellable lease term starts on 1 January 2020 and ends on 30 June 2021. The contract does not include any non-lease components, extension, termination or purchase options. The discount rate is 5% at the commencement date. As a direct consequence of the COVID-19, on 1 July 2020, A agrees to defer the lease payment originally due on 31 December 2020 to 30 June 2021. There are no other changes to the terms and conditions of the lease and hence all conditions for availing practical expedient in proposed amendment are satisfied (refer Q39 for conditions). How should B account for such deferral as per the approaches discussed in Q48?**

Response

(Note: The response below is based on exposure draft on proposed amendments to Ind AS 116 and needs to be relooked if final amendments are not in line with current draft.)

Approach 1- Account for the deferral as a negative variable lease payment

On 1 July 2020, A treats the concession as an event or condition which triggers a negative variable payment. Lessee derecognizes the part of the lease liability which is the time value of money of the lease payment deferred using the unchanged discount rate with the adjustment in profit or loss.

Lease liability immediately before the rent concession:

Present value of lease payments discounted at 5% = INR 1,15,679 $(60{,}000/(1.05)^{1/2} + 60{,}000/1.05)$

Lease liability immediately after the rent concession:

Present value of lease payments discounted at 5% = INR 1,14,286 (1,20,000/1.05)

Particulars	Dr. / Cr.	Amount
Lease liability (1,15,679-1,14,286)	Dr.	1,393
Profit or Loss	Cr.	1,393

Depreciation of the right-of-use asset continues over the remaining lease term.

Approach 2- Account for the deferral as a resolution of a contingency that fixes previously variable lease payments

The accounting under this approach would be the same as under Approach 1 above, except that the credit of INR 1,393 would be recognized as an adjustment to the right-of-use asset, rather than a credit to profit or loss.

Particulars	Dr. / Cr.	Amount
Lease liability (1,15,679-1,14,286)	Dr.	1,393
Right-of -use	Cr.	1,393

Depreciation of the revised right-of-use asset continues over the remaining lease term.

Approach 3 – Account for the deferral of lease payments as if the lease is unchanged

In this approach, Lessee A continues to account for the lease liability and right-of-use asset using the rights and obligations of the existing lease. The lease payment originally due on 31 December 2020 will remain on the balance sheet until it is settled on 30 June 2021, but the amount will not accrue interest during the deferral period. Hence, the interest expense for the six months up to 30 June 2021 will remain the same as in the original amortization schedule.

Depreciation of the right-of-use asset continues over the remaining lease term.

How we see it

The lease modification accounting would pose challenges for entities when there are multiple contracts which have been renegotiated due to coronavirus outbreak. However, the amendment proposed in Ind AS 116 would help entities to overcome those challenges by allowing entities not to apply lease modification accounting to certain renegotiations that fulfill the conditions mentioned in the proposed amendment.

8 Employee benefits

The coronavirus outbreak may significantly impact how employees of the entity are remunerated. The outbreak will also affect various estimates and actuarial assumptions that the management has been making in measurement of employee benefit obligations. For instance, there may be an impact on discount rate used to discount employee benefit obligations and future salary growth rates may no longer hold good. Entities considering layoffs might have to provide for termination benefits if they are committed to a restructuring plan on the reporting date or can no longer withdraw benefits of those offers. Entities may also have to modify their existing employee stock option plans ("ESOP") to ensure that employees are fairly compensated for the decrease in share prices.

Q51 An entity has rolled out an employee stock option plan (ESOP). Vesting conditions of ESOP include that an employee should be in employment as on 31 March 2020 and share price of the entity should achieve a certain growth as on 31 March 2020. Due to significant volatility, share price of the entity has come down and no shares are expected to vest. How should the entity account for it?

Response

Ind AS 102 *Share-based Payment* requires that market conditions upon which vesting (or exercisability) is conditioned should be taken into account when estimating the fair value of the equity instruments granted. For grants of equity instruments with market conditions, the entity is required to recognize the goods or services received from a counterparty who satisfies all other vesting conditions, irrespective of whether the market condition is satisfied.

Accordingly, subsequent accounting of the option will not change whether or not share price targets are achieved. This is because possibility of non-achievement of the share price target has already been captured in grant date fair value of the option. The entity should account for expenses in the current period based on the number of employees who have satisfied service conditions (along with other vesting conditions, if any).

Q52 Due to significant decrease in share price of the entity, it has reduced exercise price of its ESOP. How should this modification be accounted for?

Response

As the entity has reduced exercise price of the option, it will result in increase in fair value of the equity instruments granted. The entity should include the incremental fair value granted (difference between fair value, as on the modification date, of the modified equity instrument and that of the original equity instrument) in the measurement of the amount recognized for services received over the remaining vesting period.

Had such modifications increased the exercise price or otherwise reduced fair value of the option granted, the entity would have continued accounting for ESOP without taking into account such modification.

Q53 **Considering the present uncertain situations, an entity may find it difficult to make long term estimates with respect to salary growth of its employees. Can the entity segregate their assumptions into short term and long term?**

Response

Salary growth is one of the most important actuarial assumption for actuarial valuation of salary-based employee benefits such as gratuity and lease encashment. Considering the economic disruption caused by coronavirus and the corresponding lack of clarity about the longevity of the disruption, the salary growth rate assumption can become a point of discussion and debate. Further, the entity also may find it challenging to estimate this based on historical pattern of salary growth because it may not be representative in the current time.

Under the standard, it is possible to use short-term and long-term actuarial assumptions. This approach has an advantage to reflect the current situation and resultant assumption while keeping the strategic outlook of the entity in the long term.

Q54 **What possible impact can there be on actuarial valuation of employee benefits considering coronavirus?**

Response

Considering the economic disruption and significant uncertainties caused by the coronavirus outbreak, there could be numerous judgements to make in determining actuarial assumptions (such as future salary, discount rate, employee turnover rate) and employee benefits, which an employee would be entitled to. Ind AS 19 *Employee Benefits* requires actuarial assumptions to be unbiased mutually compatible and should represent the entity's best estimate of the variables that will determine the ultimate cost of providing post-employment benefits.

Any changes institutionalized by the entity in structure of employee benefits and duly agreed with the employees for the current reporting period considering the economic disruption caused by the coronavirus outbreak (such as declaration in lapse of accumulated leave balance) shall also be considered while performing the actuarial valuation.

Q55 **After reporting date, management of the entity amended the policy and decided that no carry forward of accumulated leaves will be allowed. How should the same be factored in the actuarial valuation of employee benefits on the reporting date?**

Response

Ind AS 19 requires that long-term employee benefits must be measured such that it reflects the benefits set out in the terms of the plan at the end of the reporting period. Decision of the management to change benefits after reporting date is a non-adjusting event and therefore actuarial valuation of the liability should be done without considering this development. However, the entity should evaluate if disclosure is warranted considering materiality considerations.

Q56 **When termination benefits for layoffs should be accounted for?**

Response

An entity should recognize termination benefits at earlier of:

- when it can no longer withdraw the offer of those benefits
- when it recognizes costs for a restructuring that is within the scope of Ind AS 37 and involves the payment of termination benefits

If an entity is only considering termination of employment but same has not been communicated to employees, termination benefits need not be recognized unless it has recognized restructuring provisions under Ind AS 37.

Further, even when termination plan has been communicated to employees but it does not contain sufficient details of compensation payable, number and class of employees to be terminated and expected completion date or it is likely that the significant changes to plan will be made, no provision towards termination benefits can be made.

However, if an entity has made provisions for restructuring under Ind AS 37 and such restructuring also involves payment of termination benefits, provision is required for such termination benefits.

Further, it is imperative to note that when making provisions, a distinction between post-employment benefit plans and termination benefit is required to be made. For example, when an employee is entitled to gratuity as per an existing plan, based on number of years of completion of service, it will not be covered under termination benefits.

Q57 **For measurement of net defined benefit liability (asset), an entity has been using extrapolation technique to arrive at reliable measurement for quarterly reporting purposes. Given impact of the outbreak, can entity continue with this approach under following scenarios:**

i. If there has been plan amendment, curtailment or settlement

ii. Other cases

Response

i. If there has been plan amendment, curtailment or settlement

If plan amendment, curtailment or settlement occurs, an entity should recognize and measure any past service cost, or a gain or loss on settlement. The entity should remeasure the net defined benefit liability (asset) using the current fair value of plan assets and current actuarial assumptions, including current market interest rates and other current market prices, reflecting:

a. The benefits offered under the plan and the plan assets before the plan amendment, curtailment or settlement

b. The benefits offered under the plan and the plan assets after the plan amendment, curtailment or settlement

It will not be appropriate to use extrapolation technique and valuation should, inter alia, be based on current actuarial assumptions. However, is it important to note that it is not mandatory to involve a qualified actuary in the measurement.

ii. Other cases

Ind AS 19 requires that an entity should determine net defined benefit liability (asset) with sufficient regularity. The amounts recognized in the financial statements should not differ materially from the amounts that would be determined at the end of the reporting period. In some cases, estimates, averages and computational short cuts may provide a reliable approximation. However, it is pertinent to note that the outbreak has resulted in significant market fluctuations and may have materially impacted various assumptions used for measurement of the benefit obligation (such as salary growth rate, discount rate). These developments may indicate the need for an updated valuation and extrapolation technique may not be appropriate.

How we see it

Entities are expected to make changes to their remuneration policies to address the challenges posed and uncertainties resulting from the coronavirus outbreak. Entities should carefully evaluate accounting implications of these changes. Reassessment of existing estimates and actuarial assumptions may be required. Entities should also evaluate accounting for paid absences allowed to employees during this period.

9 Provisions and contingent assets

In accordance with Ind AS 37 *Provisions, Contingent Liabilities and Contingent Assets*, provision should be recognized, when an entity has a present obligation (legal or constructive) as a result of a past event, it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation and a reliable estimate can be made of the amount of the obligation.

Hence entities will need to assess whatever action they take because of the coronavirus outbreak results in recognition of any additional provisions. One of the important considerations would be that Ind AS 37 does not allow recognition of provisions for future operating losses.

Contingent assets

Ind AS 37 requires that wherever some or all of the expenditure required to settle a provision is reimbursed by another party, the reimbursement is recognized when, and only when, it is virtually certain that reimbursement will be received if the entity settles the obligation. The amount of the provision is not reduced by any expected reimbursement. Instead, the reimbursement is treated as a separate asset and the amount recognized for the reimbursement asset is not permitted to exceed the amount of the provision.

A contingent asset is defined as a possible asset that arises from past events and whose existence will be confirmed only by the occurrence or non-occurrence of one or more uncertain future events not wholly within the control of the entity. An entity does not recognize a contingent asset because this may result in the recognition of income that may never be realized.

Q58 **An entity has incurred losses related to the coronavirus outbreak because of the shutdown of its production facilities. However, it continues to incur expenses for staff costs, rent and property taxes. It has also entered into insurance policies to reduce or mitigate the risk of loss arising from business interruption or other events. Can it recognize insurance claim receivables as an asset?**

Response

The accounting for insurance claims will differ based on a variety of factors, including the nature of the claim, the amount of proceeds and timing of loss and corresponding insurance recovery. In addition, any accounting for

> Provisions of INR 333 crores on account of COVID-19 related expenses have been provided by companies in Q4 2020

insurance proceeds will be affected by the evaluation of coverage for that specific type of loss in a given situation, and an analysis of the ability of an insurer to satisfy a claim.

Careful analysis of the terms and conditions of an entity's business interruption policies will be required due to a wide variety of terms relating to the nature and level of losses covered.

Recognition of insurance recovery will only be appropriate when its realization is virtually certain, in which case, the insurance recovery is no longer a contingent asset. Although 'virtually certain' is not defined in Ind AS 37, it is certainly a much higher hurdle than 'probable'.

Hence if it is virtually certain that the entity will be compensated for at least some of the consequences of the coronavirus outbreak under a valid insurance policy, then insurance recovery shall be recognized as an asset.

Further 'netting off' is not allowed in balance sheet and hence insurance recovery asset is to be presented separately from any provision.

Onerous contract provisions

An onerous contract is a contract in which the unavoidable costs of meeting the obligations under the contract exceed the economic benefits expected to be received under it. The unavoidable costs under a contract reflect the least net cost of exiting from the contract, which is the lower of the cost of fulfilling it and any compensation or penalties arising from failure to fulfil it. If an entity has a contract that is onerous, Ind AS 37 requires the entity to recognize and measure the present obligation under the contract as a provision. Before a separate provision for an onerous contract is established, an entity recognizes any impairment loss that has occurred on assets dedicated to that contract.

Refer section 5 for further details on impairment considerations.

Q59 **A manufacturing entity has contracts to sell goods at a fixed price. However, because of the coronavirus outbreak, Government has announced shutdown of its manufacturing facilities and hence an entity cannot deliver the goods itself without procuring them from a third party at a significantly higher cost. Also, the entity is required to pay penalty, if it does not deliver goods. Whether onerous contract provision is required in this case?**

Response

In the given case, contracts should be reviewed to determine if there are any special terms that may relieve an entity of its obligations (such as, force majeure) and it may involve legal interpretation of various clauses.

If the entity concludes that it is not relieved of its obligation to deliver goods at fixed price, then provision for the onerous contract will be recognized at lower of the penalty for terminating the contract or the present value of the net cost of fulfilling the contract (such as the excess of the cost to procure the goods over the consideration to be received and any other cost for fulfilling the contract).

Q60 **An entity has committed itself to lease arrangement expected to commence at a future date. Considering the economic downturn due to coronavirus outbreak, property rentals are significantly reduced and entity estimates that unavoidable costs of meeting the obligations under the contract exceed the economic benefits expected to be received. This results in such lease arrangement to becoming onerous. Does Ind AS 37 apply to such situations?**

Response

Ind AS 37 provides that when a particular item is covered by any other standard, that specific standard should be applied to those provisions and not Ind AS 37.

However, Ind AS 37 applies to leases which have not been recognized in financial statements because commencement date for those contracts may not have come yet.

Where an entity has entered into a lease agreement to take assets on lease from a future date and considering current situation expects unavoidable costs of meeting obligations under the lease contract to exceed economic benefits, it should consider it onerous and make provision as per Ind AS 37.

Future operating losses

While affected entities may account for some effects of the outbreak in the current period, other direct and indirect effects such as losses or lost revenue, may need to be accounted for in subsequent periods. Entities may anticipate losses that are directly or indirectly related to the current outbreak. These might include losses related to significant reduction in demand, supply chain disruptions and losses due to an overall decline in economic output.

Future operating losses do not meet the definition of a liability and, therefore, should not be recognized until they are incurred; however, affected entities may need to consider whether additional disclosures are required.

How we see it

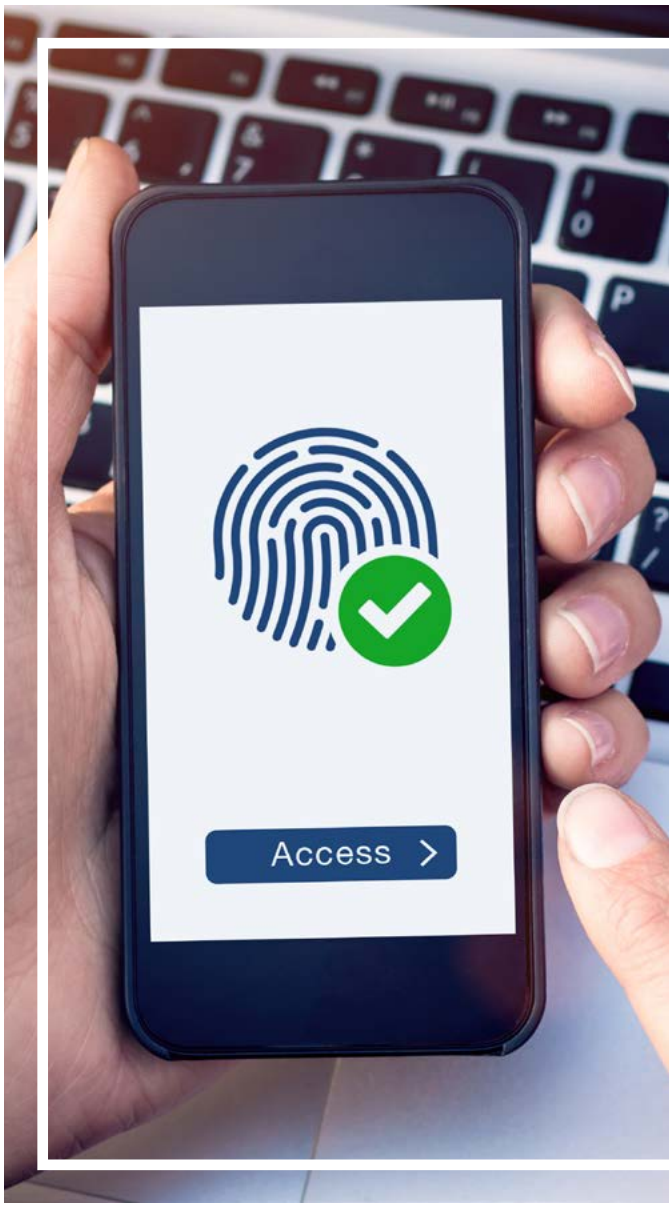
In assessing unavoidable costs of meeting the obligations under a contract at the reporting date, entities, especially those with non-standardized contract terms, need to carefully identify and quantify any compensation or penalties arising from failure to fulfil it.

10 Government grants

Ind AS 20 applies to the accounting for, and the disclosure of, Government grants and to the disclosure of other forms of Government assistance. The distinction between Government grants and other forms of Government assistance is important because the standard's accounting requirements only apply to the former. Government grants are transfers of resources to an entity in return for past or future compliance with certain conditions relating to the entity's operating activities. The purpose of Government grants, which may be called subsidies, subventions or premiums, and other forms of Government assistance is often to encourage a private sector entity to take a course of action that it would not normally have taken if the assistance had not been provided.

Recently many countries' Governments, agents or similar bodies have introduced (or are expected to introduce) relevant measures to assist entities in response to the coronavirus. These measures include direct subsidies, tax exemptions, tax reductions and credits, extended expiry period of unused tax losses, reduction of public levies, rental reductions or deferrals and low-interest loans.

Whilst the benefit of a low-interest loan would be accounted for under Ind AS 109 and Ind AS 20, not all these measures are accounted for as Government grants. For example, a reduction of income tax is accounted for under Ind AS 12 *Income Taxes* (Refer section 11); and rental reductions or deferrals may be accounted for under Ind AS 116 Leases (Refer section 7). Accordingly, entities should analyse all facts and circumstances carefully to apply the relevant Ind AS.



Q61 If the Government provides lease concessions due to the coronavirus outbreak as lessor, should the same be accounted for as Government grant or lease modification by lessee?

Response

Ind AS 20 defines Government grants as assistance by Government in the form of transfers of resources to an entity in return for past or future compliance with certain conditions relating to the operating activities of the entity. Further, Ind AS 116 defines lease modification as a change in the scope of a lease, or the consideration for a lease, that was not part of the original terms and conditions of the lease.

If the lease concession given by Government is dependent on compliance with certain conditions and it is given in its capacity as Government then it should be accounted as Government grant. However, if the lease concession is given by Government for a particular contract and is not applicable in general then it should be accounted as lease modification.

Q62 As a relief measure to Corporates due to the outbreak, the Government has allowed certain entities to delay payment of Goods and Service Tax ("GST") collected on their sales up to 5 years. GST, so collected, to be paid by entities after 5 years. How this assistance should be recorded?

Response

GST amounts retained by the entity are required to be paid after 5 years making this arrangement similar in nature to interest free loans. Accordingly, this would be initially accounted for as a financial liability under Ind AS 109 and be measured at fair value. The entity would determine value of Government assistance by comparing the amounts

retained to the fair value of 5-year loan at market rate of interest.

On initial recognition, the initial fair value of the loan is the present value of the future payment of GST amounts, discounted using the market rate of interest for similar loan with term of 5 years. The difference between the total GST collection so deferred and initial fair value so determined shall be treated as Government grant. This would be treated as a Government grant only when there is reasonable assurance that the entity will meet the terms for benefit of such arrangement, if any.

Government grants must be recognized in profit or loss on a systematic basis over the periods in which the entity recognizes as expenses the related costs for which the grants are intended to compensate. In cases where a grant relates to expenses or losses already incurred, or for the purpose of giving immediate financial support to the entity with no future related costs expected to be incurred, the grant should be recognized in income when it becomes receivable.

In cases where such grants relating to coronavirus outbreak are given to entities without any specified conditions, grant can be recognized at the time when it is reasonably certain that the grants will be received. Nevertheless, it is important to note that the receipt of a grant does not of itself provide conclusive evidence that the conditions attaching to the grant have been, or will be, fulfilled.

Q63 Considering financial difficulties caused by the coronavirus outbreak, the Government may agree to modify the terms of a loan such as extension of loan term or reduction of interest rate for a few years. Would such modifications to loan terms be accounted for under Ind AS 109 or as Government assistance under Ind AS 20?

Response

A substantial modification to the terms of the existing liability, or a part of it, should be accounted for as an extinguishment of the original financial liability and the recognition of a new financial liability. Ind AS 109 regards the terms of exchanged or modified debt as "substantially different" if the net present value of the cash flow under the new terms (including any fees paid net of fees received) discounted at the original effective interest rate is at least 10% different from the discounted present value of the remaining cash flows of the original debt instrument. If the modification is not substantial, the entity needs to recognize an immediate gain or loss when the cash flows are modified, and the original liability is not derecognized but stands at modified value.

If the Government agrees for modification of original loan provided to the entity which can be considered as substantial modification under Ind AS 109, the entity needs to derecognize the original liability and recognize the new loan liability based on revised terms. The difference if any shall be treated as Government grant as assistance.

If the Government agrees for modification of original loan provided to the entity which is not substantial modification under Ind AS 109, the resulting gain out of modification i.e. the difference between the original liability as per original terms and as per modified terms, should be recorded as Government grant.

Government grants must be recognized in profit or loss on a systematic basis over the periods in which the entity recognize as expenses the related costs for which the grants are intended to compensate. In cases where a grant relates to expenses or losses already incurred, or for the purpose of giving immediate financial support to the entity with no future related costs expected to be incurred, the grant should be recognized in income when it becomes receivable.

However, the entity should evaluate if disclosure is warranted considering materiality considerations.

How we see it

Whether Ind AS 20 should be applied depends on the facts and circumstances of the specific measures implemented by the Government, including Government agencies and similar bodies. Entities need to analyze all facts and circumstances carefully to determine the appropriate accounting treatment.

11 Income taxes

In response to the coronavirus pandemic, many Governments are contemplating measures to provide aid and economic stimulus. These measures may include deferring the due dates of tax payments or other changes to their income and non-income-based tax laws. Entities need to consider the impacts of these legislative changes on their accounting for income taxes.

Ind AS 12 *Income Taxes* requires current tax liabilities and assets for current and prior periods to be measured at the amount expected to be paid to (or recovered from) the taxation authority, using the tax rates and laws that were enacted, or substantively enacted, by the end of the reporting period. Deferred tax assets and liabilities must be measured at the tax rates expected to apply to the period when the asset is realized or the liability is settled, also using the tax rates and laws that were enacted, or substantively enacted, by the end of the reporting period.

Q64 Government has announced the intention to give tax reliefs but it is yet to be enacted in form of law. Could such reliefs be considered for determining tax assets and tax liabilities?

Response

In some jurisdictions, announcements of tax rates (and tax laws) by the government have the substantive effect of actual enactment. In such circumstances, tax assets and liabilities are measured using the announced tax rate. However, this is not always the case and an entity would need to consider when the tax concessions (e.g., reduced tax rates) become substantively enacted in their jurisdiction. For example, in India, the enactment date is date when the bill becomes the law, which is generally upon the presidential signature and notification thereupon.

However, it may be substantively enacted if it were to be approved either through an ordinance or by way of an approval in the parliament.

Determining the enactment date in other jurisdiction (jurisdiction of entity's subsidiaries, associates and joint ventures) need to be considered by the entity while preparing consolidated financial statements with an understanding of legislative process in those jurisdictions.

Q65 If Government relief in tax laws have implications on tax payable or refundable of prior period, how should it be accounted?

Response

The tax effect of change in tax law or rates or rules around utilization of tax losses of prior periods may have impact on taxes payable or refundable of prior periods. Any tax expense or benefit arising from such change and having impact on taxes payable or refundable of prior period should be recorded in the current year.

Q66 **Does the current situation warrant the reassessment of deferred tax assets?**

Response

Entities affected by current market conditions of coronavirus pandemics may be incurring unexpected losses and may need to reevaluate and change their conclusions about the realizability of their deferred tax assets. Future realization of deferred tax assets ultimately depends on the existence of sufficient taxable income of appropriate character during the carryforward period. Recent cumulative losses or the expectations that an entity will have cumulative losses constitutes significant negative evidence about the realizability of the deferred tax assets.

Management should also consider whether the disclosures made in the notes of the financial statements regarding the realizability of entity's deferred tax assets are sufficient.

How we see it

Entities need to determine whether changes to tax rates and laws as part of Government responses to the coronavirus outbreak, were substantively enacted as of the reporting date. The characteristics of any tax relief or rebates received by the Government need to be carefully assessed in order to determine whether they should be accounted for as a reduction to the income tax expense, or the receipt of a Government grant. Uncertainties relating to income taxes arising from these new Government measures will require entities to consider whether they should recognize and measure current and/or deferred tax assets or liabilities at a different amount.

12 Other matters

Due to the coronavirus situation, most of the existing management judgements and estimates will need to be assessed while preparing financial statements. Further, an entity needs to assess if the present economic situation is going to have a temporary impact on its operations or medium to long term impacts. It will enable evaluation of the application of certain accounting policies.

Q67 Can entity continue to capitalize the borrowing cost when the construction is disrupted due to current coronavirus situation?

Response

Ind AS 23 *Borrowing Costs* requires capitalization of borrowing costs to be suspended during extended periods in which active development of a qualifying asset is suspended. Ind AS 23, inter alia, further states that an entity does not suspend capitalizing borrowing costs when a temporary delay is a necessary part of the process of getting an asset ready for its intended use or sale. It also includes an example in this regard that, for example, capitalization continues during the extended period that high water levels delay construction of a bridge, if such high water levels are common during the construction period in the geographical region involved.

From the above, it seems that the temporary delay due to coronavirus outbreak is not a necessary part of process of getting asset ready for its intended use and is of not an event which is of common nature. So, borrowing costs incurred during such period are costs incurred for holding partially completed assets rather than cost of undertaking activities for developing the project and therefore, should not be capitalized.

Q68 What will be the potential implications on depreciation charge of Property, Plant and Equipment ("PP&E") due to under-utilization or over utilization arising from the coronavirus situation?

Response

PP&E is required to be depreciated when it is available for use i.e. in the location and condition necessary for it to be capable of operating in a manner intended by the management. An entity does not stop depreciating an asset merely because it became idle or has been retired from active use unless the asset is fully depreciated.

Unless current coronavirus situation warrants any substantial change in useful life of the assets or the pattern in which economic benefits would be realized from such asset, the entity shall continue to depreciate the assets as per their current accounting policy and estimate of useful lives.

Q69 Does changing liquidity position of fund and investment market have any implications for Cash and Cash Equivalent ("CC&E") position of an entity?

Response

Ind AS 7 defines CC&E as short term highly liquid investments that are readily convertible to known amount of cash and which are subject to insignificant risk of changes in value. The entity needs to relook at their CC&E components from two aspects in current situation:

1. Coronavirus outbreak has resulted in the value of some money market and other funds declining more than insignificantly. Considering the risk of significant change in value, an entity needs to evaluate if such funds still meet the definition of CC&E.
2. Some money market funds include clauses which allow the fund manager to restrict redemption in unlikely events, one of which might be the result of coronavirus. Whether any such restriction on redemption in current terms defies the nature of investment in fund as CC&E.

Q70 How should an entity account for Corporate Social Responsibility ("CSR") expenditure on account of the coronavirus outbreak which is in excess of minimum expenditure required for that year as per the Companies Act, 2013 (CA 2013)?

Response

Presently, CA 2013 does not allow any excess amount spent on CSR over the required threshold to be carried forward to subsequent years to be set off against CSR compliance of future years. It is pertinent to note that CSR provisions of CA 2013 has been amended by the Companies (Amendment) Act, 2019 and CSR spend is made mandatory and punitive in the revised Act and any unspent amount is required to be transferred to specified fund within 6 months from the expiry of the financial year (subject to exception of specified ongoing projects). The amendment, however, has not been notified yet and hence the following discussion is in light of present provision of CA 2013 for CSR spend. This needs to be reassessed if Companies (Amendment) Act, 2019 is notified.

Under current provisions of CA 2013, CSR provisions do not meet definition of obligating events and when an entity is unable to spend recommended amount, it is not required to make provision for the shortfall, but only requires disclosure in board report specifying the reasons for not spending the amount.

There is no clarification or provision which permits excess amounts incurred for the coronavirus outbreak to be offset against obligation of any future period. Excess amount does not meet definition of an asset as provided in 'Framework for the Preparation and Presentation of Financial Statements in accordance with Indian Accounting Standards', issued by ICAI and therefore, entity should charge such excess amount to statement of profit and loss in period of incurrence.

Q71 Can expenditure incurred on salary / wages to employees and workers (including casual and daily wage workers) during lockdown period be treated as CSR expenditure? Would payment of ex-gratia to temporary /casual /daily wage workers qualify as CSR expenditure?

Response

Ministry of Corporate Affairs ("MCA") has clarified payment of salary/wages to employees and workers, including contract labour, casual /daily wage workers, during the lockdown period shall not qualify as admissible CSR expenditure.

CSR projects or programs or activities that benefit only the employees of the entity and their families are not considered as CSR activities under CA 2013 (The Companies (Corporate Social Responsibility Policy) Rules, 2014). However, MCA has stated that payment of ex-gratia over and above the disbursement of wages to temporary / casual /daily wage workers, specifically for the purpose of fighting coronavirus, shall qualify as CSR expenditure as a onetime exception. However, there should be an explicit declaration to that effect by the board of the company, which is duly certified by the statutory auditor.

As exception has been made only in case of temporary/casual/daily wage earners, we are of the view same should not be applied by analogy to ex- gratia paid to other employees of the entity.

Q72 Can entities engaged in production of sanitizers or protective or critical medical equipment (such as ventilators) claim it as CSR expenditure under the current situation? Will answer differ if such an activity is being undertaken by an entity engaged in other business operations (such as automobile manufacturing)?

Response

CSR activities do not include the activities undertaken in pursuance of normal course of business of an entity (The Companies (Corporate Social Responsibility Policy) Rules, 2014). Accordingly, expenditure incurred on production of sanitizers/protective/ critical medical equipment will not qualify as CSR expenditure. Similar principles will apply where such activities are being undertaken by an entity engaged in other business activities.

However, where entities are supplying such goods free of cost or at below cost, then same may require careful evaluation for its classification as CSR expenditure within scope of items specified in schedule VII to CA 2013. It is pertinent to note that MCA has clarified that items in the schedule VII are broad based and may be interpreted liberally for this purpose.

Q73 As per recent announcement by the Government, private companies which list Non-Convertible Debentures ("NCDs") on stock exchanges are not to be regarded as listed companies. How this will impact the applicability of Ind AS to: i) a private company which currently follows Ind AS only because its NCDs are listed and ii) a private company which is currently not required to follow Ind AS but may go for listing of NCDs in future?

Response

As per the notification of MCA dated 16 February 2015 on the rules of applicability of Ind AS, all companies whose equity or debt securities are listed or are in the process of being listed on any stock exchange should prepare their financial statements as per Ind AS.

The said notification also states that once a company starts preparing its financial statements as per Ind AS then it shall be required to follow Ind AS for all the subsequent financial statements even if any of the criteria specified in the rules does not subsequently apply to it.

With respect to the announcement made by the Government on the listing status of private companies, an amendment has been proposed in the Companies (Amendment) Bill, 2020 to modify the definition of a listed company as per Companies Act, 2013 to give effect to the announcement made by the Government. However, the amendment has not been notified yet. Once the amendment is notified, it may impact the applicability of Ind AS to private companies with listed NCDs as follows:

A private company which currently follows Ind AS only because its NCDs are listed

A private company which already follows Ind AS at the time of notification of above amendment only because its NCDs are listed, will to continue preparing its financial statements under Ind AS. This is because once the company gets covered under Ind AS, it continues to follow Ind AS even if the criteria for applicability of Ind AS are subsequently not met as mentioned in the rules of applicability of Ind AS stated above.

A private company which is currently not required to follow Ind AS but may go for listing of NCDs in future

It is to be noted that the amendment has been proposed in the definition of listed companies as per Companies Act, 2013. However, the rules for applicability of Ind AS does not refer to the definition of listed company as per Companies Act, 2013 rather it states that Ind AS is applicable to companies whose equity or debt securities are listed or are in the process of being listed on any stock exchange. Hence, there is an ambiguity that, while assessing the applicability of Ind AS, whether an entity shall consider the amendment made to the definition of listed companies or not. Considering the ambiguity, regulator should address the concern while finalizing the Bill. (However, Ind AS may be applicable to such company if it meets any other criteria of applicability of Ind AS such as net worth crossing the threshold or listing of equity shares, etc.).

13 Key presentation and disclosures

An affected entity's disclosures will depend on the magnitude, duration and nature of the effects on its business. Entities will need to closely monitor developments and assess the implications for their businesses.

Following are some of the key disclosures which entities may need to evaluate:

Financial statement disclosure requirements

Ind AS 1 requires disclosure of information about the assumptions concerning the future, and other major sources of estimation uncertainty at the end of the reporting period, that have a significant risk of resulting in a material adjustment to the carrying amounts of assets and liabilities. This may include, non-current assets subject to impairment, within the next financial year (with the exception of assets and liabilities measured at fair value based on recently observed market prices). The disclosures are required to be presented in a manner that helps users

of financial statements to understand the judgements that management makes about the future and about other key sources of estimation uncertainty. The nature and extent of the information provided will vary according to the nature of the assumption and other circumstances.

Examples of the types of disclosures that an entity is required to make include:

- The nature of the assumption or other estimation uncertainty
- The sensitivity of carrying amounts to the methods, assumptions and estimates underlying their calculation, including the reasons for the sensitivity
- The expected resolution of an uncertainty and the range of reasonably possible outcomes within the next financial year with respect to the carrying amounts of assets and liabilities affected
- An explanation of changes made to past assumptions concerning those assets and liabilities, if the uncertainty remains unresolved

When it is impracticable to disclose the extent of the possible effects of an assumption or other source of estimation uncertainty at the end of a reporting period, the entity discloses that it is reasonably possible, based on existing knowledge, that outcomes within the next financial year that are different from assumptions used could require a material adjustment to the carrying amount of the asset or liability affected.

Q74 An entity may incur various losses because of the coronavirus outbreak, including liquidated damages, fixed cost during factory shut down, and impairment of financial / non- financial asset. Some of these losses may be material in nature. Could they be disclosed as exceptional items?

Response

Neither Ind AS nor Schedule III to the Companies Act, 2013 define the term 'exceptional item'. However, Schedule III (Division II and III) to the Companies Act, 2013 requires presentation of exceptional items on the face of the statement of profit and loss. Further, SEBI requires the listed company to follow Schedule III format for presentation of financial results.

As per Ind AS 1, when items of income or expense are material, an entity shall disclose their nature and amount separately. Entities are permitted to present additional line items, headings and subtotals in the statement of profit and loss, when such presentation is relevant to an understanding of the entity's financial performance. Further, Ind AS 1 allows expenses to be subclassified in the statement of profit and loss on the basis of frequency, potential for gain or loss and predictability. The two aspect which may lead to the conclusion that whether an item can be considered as an exceptional item are materiality and its predictability.

Given the specific requirement of SEBI and Schedule III, it may not be inappropriate to disclose a material and non-recurring item as an exceptional item on the face of profit and loss. However, it may be challenging to segregating an expense between exceptional and non-exceptional as the expense may have been caused by both exceptional and non-exceptional factors. Further, it would also result into mixed presentation, i.e., nature wise as well as functional classification. Hence, preferred option is to disclose such items in notes to the financial statements in detail.

Fair value measurement

To meet disclosure objectives of Ind AS 113, entities will need to consider making related disclosures that could reasonably be expected to influence decisions that the primary users of general-purpose financial statements would make based on the financial statements. Depending on the facts and circumstances of each case, disclosure may be needed to enable users to understand whether or not the outbreak has been considered for the purpose of FVM. Users should understand the basis for selecting the assumptions and inputs that were used in the FVM and the related sensitivities.

Given the outbreak is evolving, entities are also reminded to consider the disclosure requirements from other standards that are relevant to FVM, such as Ind AS 10 on subsequent events and developments when asset values are significantly impacted subsequent to the reporting date.

Financial instruments

Entities with concentrations of risk, face greater risk of loss than other entities. Paragraph 34(c) of Ind AS 107 requires that concentration of risk should be disclosed if not otherwise apparent from other risk disclosures provided.

Therefore, entities should consider including the following information:

- A description of how management determines concentrations of risk
- A description of the shared characteristic that identifies each concentration (such as, counterparty, geographical area, currency or market). For instance, the shared characteristic may refer to geographical distribution of counterparties by groups of countries, individual countries or regions within countries and/or by industry
- The amount of the risk exposure associated with all financial instruments sharing that characteristic

Entities that have identified concentrations of activities in areas or industries affected by the outbreak (such as, the airline, hospitality and tourism industries) that have not previously disclosed the concentration because they did not believe that the entity was vulnerable to the risk of a near-term severe impact, should now reconsider making such a disclosure.

Similarly, liquidity risk in the current economic environment is increased. Therefore, it is expected that the disclosures required under Ind AS 107 in this area will reflect any changes in the liquidity position as a result of the coronavirus outbreak. Entities should be mindful that this disclosure is consistent with their assessment of the going concern assumption.

Entities will also need to assess impact on disclosures relating to interest rate risk, foreign currency risk and market risk. Although entities are currently providing these disclosures, but it may now reassess on the extent of details to be provided for this disclosure, since coronavirus outbreak may have impact on these risks.

Events after the reporting period

If the management concludes that an event is a non-adjusting event, but the impact of it is material, the entity is required to disclose the nature of the event and an estimate of its financial effect. For example, it may have to describe qualitatively and quantitively how the market volatility subsequent to year-end has affected its equity investments and governmental measures imposed on sporting and social activities and border controls have affected or may affect its operations, etc. If an estimate cannot be made, then the entity is required to disclose that fact.

Disclosure of material impact of COVID-19 pandemic on listed entities under SEBI (Listing Obligations and Disclosure Requirements) Regulations, 2015 ("LODR Regulations"/"LODR")

SEBI has issued a circular encouraging entities to evaluate the impact of the COVID-19 pandemic on their business, performance and financials, both qualitatively and quantitatively, to the extent possible and disseminate the same. SEBI circular provides an illustrative list of information that listed entities may consider disclosing, subject to the application of materiality. Such list is reproduced below:

- Impact of the COVID-19 pandemic on the business
- Ability to maintain operations including the factories/units/office spaces functioning and closed down
- Schedule, if any, for restarting the operations
- Steps taken to ensure smooth functioning of operations
- Estimation of the future impact of COVID-19 on its operations
- Details of impact of COVID-19 on listed entity's –
  - Capital and financial resources
  - Profitability
  - Liquidity position;
  - Ability to service debt and other financing arrangements
  - Assets
  - Internal financial reporting and control
  - Supply chain
  - Demand for its products/services
- Existing contracts/agreements where non-fulfilment of the obligations by any party will have significant impact on the listed entity's business
- Other relevant material updates about the listed entity's business

The above list is only illustrative and not exhaustive. Further, to have continuous information about the impact of COVID-19 on operations, listed entities may provide regular updates, as and when there are material developments.

Additionally, while submitting financial statements under Regulation 33 of the LODR, listed entities may specify/include the impact of the COVID-19 pandemic on their financial statements, to the extent possible.

Q75 Outbreak has brought in significant volatility in financial result of many entities. Can an entity elect to disclose alternate performance measures ("APM") such as incremental coronavirus cost?

Response

Ind AS 1 requires entities to clearly identify and distinguish Ind AS financial statements from other information in the same published document. It generally requires the presentation of specific line items, but only if these are material. Further entities are required to present additional line items and subtotals, when such presentation is relevant to the understanding of the entity's financial position or financial performance. If so, Ind AS 1 sets out certain requirements, including that they are labelled in a manner that makes the line items that constitute a subtotal clear and understandable and that they are not displayed with more prominence than the subtotals and totals required by Ind AS.

Hence entity may elect to disclose alternate performance measures such as incremental coronavirus costs in its financial statements. There are various ways that an entity may elect to provide information on the impact of the coronavirus outbreak through APMs, additional line items and additional disclosures. For example, entities may decide to present additional line items or new APMs in their primary financial statements, disclose new or adjusted APMs in the notes to their financial statements or disclose quantitative estimates or qualitative explanations of the impact of the coronavirus outbreak in the notes without using APMs. Moreover, entities may elect to use new or adjusted APMs either inside or outside their financial statements or both.

As with the requirement to include additional line items or subtotals, entities must apply judgement in considering which information in relation to APMs is relevant to an understanding of the financial statements. Further, entities should also apply judgement and determine till what subsequent period it should continue disclosure of such APMs, considering its relevance to the understanding of the entity's financial position or financial performance.

Q76 The government has proposed amendment to definition of micro small and medium enterprises ("MSME"). For making disclosures required by Schedule III and the Micro, Small and Medium Enterprises Development Act, 2006 for the year ended 31 March 2020, should an entity consider revised classification?

Response

As a part of the COVID-19 related announcements by the Finance Minister on 13 May 2020, the definition of MSME is modified as follows:

- The threshold for investment in criteria for classification of micro, small and medium enterprises is increased
- Additional criteria for turnover is added

The above amendment is effective from 1 July 2020. If an entity's financial statements were not approved for issue by the date when the above announcement was made, then this will be an event after the reporting period. Events after the reporting period can either be adjusting and non-adjusting events and the distinction between these two events is based on whether the event provides evidence of conditions that existed at the end of the reporting period or not. In this case, there was no evidence of the change in definition of MSME as at 31 March 2020 and change is effective after the reporting date. Hence, this will be a non-adjusting event and no adjustment is required to be made in the financial statements for the year ended 31 March 2020. However, if such amendment is considered as a material non-adjusting event for an entity then that entity should make necessary disclosures as required by Ind AS 10.

Further, from the effective date of above amendment, an entity might also have financial impacts (like interest on delayed payments to micro and small enterprises) and working capital impacts (like payments required to be done within due dates to micro and small enterprises) on account of above changes in definition of MSME.

How we see it

Entities need to consider the magnitude of the disruptions caused by the outbreak to their businesses and adequately discloses the information about those assets and liabilities that are subject to significant estimation uncertainty, in order to provide users with a better understanding of the financial impact.

Entities need to ensure that effective processes are in place to identify and disclose material events after the reporting period which could reasonably be expected to influence decisions that the primary users of general-purpose financial statements make based on those financial statements.

14 Book closure and audit

As entities are preparing for the reporting period close they may face challenges with respect to period end activities and audit of their financial statements. The events that have happened over the last few weeks were unexpected and entities may have to make changes to their plans for financial statement closure and audit of financial statements. Entities will have to determine their ability to meet financial reporting and filing requirements with various authorities and comply with other legal and regulatory requirements. Entities will have to ensure that financial reporting, compliance and auditing procedures continue to be adequately performed through a combination of physical and remote working procedures and also evaluate options to perform alternative procedures to facilitate timely collection, processing and reporting of information for book closure and audit of financial statements. Entities will have to be prepared for the anticipated changes in audit procedures such as changes to materiality, scope, physical verification of inventories and other additional procedures.

Entities whose equity shares or convertible securities are listed and entities whose non-convertible debentures (NCD) or non-convertible redeemable preference shares (NCRPS) or commercial papers (CPs) are listed / proposed to be listed should also take into consideration the relief given by Securities and Exchange Board of India ("SEBI") with respect to timing of filing of the financial results for the quarterly/ half yearly / annual results for the quarter / half year / financial year ended on 31 March 2020.

The relief given by SEBI in filing of financial results is summarized below:

Regulation	Filing		Relaxation		
	Frequency	Due within	Due date	Extended date*	Period of relaxation
Regulation 33 (listed equity shares or convertible securities)	Quarterly	45 days from end of quarter	15 May 2020	31 July 2020	1 month and 45 days
Regulation 33 (listed equity shares or convertible securities)	Annual	60 days from end of financial year	30 May 2020	31 July 2020	2 months
Regulation 52 (listed NCD or NCRPS) or listed CPs	Half yearly	45 days from the end of half year	15 May 2020	31 July 2020	1 month and 45 days

Regulation	Filing		Relaxation		
	Frequency	Due within	Due date	Extended date*	Period of relaxation
Regulation 52 (listed NCD or NCRPS) or listed CPs	Annual	60 days from end of financial year	30 May 2020	31 July 2020	2 months

* As per the earlier circulars issued by SEBI on 19 March 2020 and 23 March 2020 for regulation 33 and regulation 52 respectively, the extension was given up to 30 June 2020. However, as per the circular issued by SEBI on 24 June 2020, extension of one more month is granted. Hence the revised extended date is 31 July 2020.

In line with the relaxations given by SEBI, the Reserve Bank of India has also given relaxation for finalization of audited accounts by Non-Banking Financial Companies (NBFCs). As per the relaxation, NBFCs which were required to finalize their balance sheet within a period of three months from the date to which is pertains can now finalize their balance sheet within a period of three months from the date to which it pertains or any date as notified by SEBI for submission of financial results by listed entities.

(Note: As of now, there is no update from the regulators regarding relaxations in timelines for the publishing of quarterly results for 30 June 2020. However, considering the extension of relaxation for the publishing of results for the period ended 31 March 2020 this will be an important area to look out for)

Relaxation from publishing quarterly consolidated financial results under regulation 33(3)(b) of the LODR for certain categories of listed entities

Listed entities which are banking and / or insurance companies or having subsidiaries which are banking and / or insurance companies may submit consolidated financial results under regulation 33(3)(b) for the quarter ending June 30, 2020 on a voluntary basis. However, they shall continue to submit the standalone financial results as required under regulation 33(3)(a) of the LODR. If such listed entities choose to publish only standalone financial results and not consolidated financial results, they shall give reasons for the same.

Apart from above, Ministry of Corporate Affairs (MCA) has given certain relaxations as follows:

Relaxation in requirements of holding Board meetings

MCA has given relaxation in the requirement of holding Board meetings with physical presence of directors under section 173 (2) r/w rule 4 of the Companies (Meetings of Board and its Powers) Rules, 2014 for approval of the annual financial statements, Board's report, etc. Such meetings may till 30 September 2020

> Audit reports of 93 companies included emphasis of matter paragraph in Q4 2020

(earlier the relaxation was up to 30 June 2020, now the same has been extended by notification of MCA dated 23 June 2020) be held through video conferencing or other audio-visual means. This relief is available to both listed and unlisted entities.

Relaxation in holding Extraordinary General Meetings

MCA has allowed listed entities or entities with 1,000 shareholders or more which are required to provide e-voting facility under the Companies Act, 2013 to conduct Extraordinary General Meetings (EGM) through video conferencing or other audio-visual means and e-Voting. For other entities, a highly simplified mechanism for voting through registered emails has been put in place for easy compliance. The relaxation is given for holding of EGM which is considered unavoidable and is to be conducted on or before 30 June 2020. Entities may refer to the detailed circular MCA circular no -14/2020 dated 8 April 2020 and MCA circular no -17/2020 dated 13 April 2020 in this regard.

Relaxation in holding Annual General Meetings by companies whose financial year has ended on 31 December 2019

Companies whose financial year has ended on 31 December 2019 can hold their Annual General Meetings (AGM) for such financial year within a period of nine months from the closure of the financial year (i.e., by 30 September 2020).

Relaxation in holding AGM by video conferencing or other audio-visual means

Companies are allowed to conduct their AGM through video conferencing or other audio-visual means during the calendar year 2020, subject to the fulfillment of certain conditions. Companies may refer to the General Circular no. 20/2020 dated 5 May 2020 issued by MCA for the details of conditions required to be fulfilled to avail the relaxation. Companies which are unable to conduct their AGM in accordance with the framework provided in such circular may consider applications for extension of AGM at suitable point of time before the concerned Registrar of Companies.

Q77 What could be alternatives to performance of physical verification of inventory as on reporting date because of lock-down? Further, what if the statutory auditor is not able to be present at the time of inventory verification because of the lockdown?

Response

Entities may determine to perform physical verification of inventories on a subsequent date after the period end date in consultation with their statutory auditors. They could also perform rollback procedures to give comfort to their statutory auditors with respect to the inventory that is recorded as at the reporting date. However, entities will have to be mindful of the fact that waiting to perform physical verification of inventory in the current environment presents a high degree of risk due to the uncertainty on the timing of when things will return to business as usual.

Further, in case statutory auditors are not able to be present at the time of inventory verification then following options may be evaluated in consultation with statutory auditors to give comfort to them in their audit of the financial statements:

- Obtain assistance from internal auditor, whose work can be used by the statutory auditors In case the team performing the statutory audit is at a far location then obtain assistance from local team of the statutory auditors who can be present at the location of inventory.
- Obtain assistance from an external party (such as, an independent chartered accountant firm in that location)

Q78 What approach entities may adopt if they are not able to send the signed balance confirmation requests to third parties on letterheads of the entity?

Response

During this crisis time, entities may explore options of sending the electronic confirmation requests in consultation with their statutory auditors. The confirmation request should clearly indicate the name, address and other identifying information of the requesting entity. The confirmations may be sent in an electronic file format or alternatively the confirmation requests can be prepared on the body of an e-mail to be sent to third parties. Entities may decide the appropriate method in consultation with their statutory auditors. The auditors are required to follow mandatory standards on Auditing notified under Section 143(10) of the Companies Act, 2013.

Q79 Which are some of the best practices in this critical time to address challenges faced during closure of financial statements?

Response

Entities can adopt following practices to address challenges faced in closure of financial statements:

- Re-draw your financial statement close calendar and agree time-lines with respective stakeholders
- Compile list of all areas involving key estimates and judgements and identify data dependencies
- Communicate with your vendors and customers for performing balance confirmations electronically
- Evaluate the need to reassess estimates used in your critical estimation areas like expected credit loss, inventory
- obsolescence, onerous contracts evaluation etc.
- Plan to perform inventory rollback procedures to get comfortable with inventory valuation as at the period-end
- Prepare overall plan for book close, assigning key responsibilities, with contingency arrangements built in
- Discuss with auditors their plan for audit, their requirements and timelines

Q80 What should be the continuity plan for the finance function to complete closure of financial statements and audit of the same within prescribed timelines in situations like the coronavirus outbreak?

Response

To ensure that the finance function operates effectively during situations like the coronavirus outbreak, entities may focus on digitalizing the process of financial statement closure as well as digitalizing the audit process. In particular, entities may adopt following as part of their continuity plan for the finance function during the time of crisis like coronavirus:

- Set up a virtual command center to manage communications between relevant stakeholders
- Ensure VPN capacity to enable remote access.
- Re-sequence your close calendar to take into account likely delays in normal close activities. Some activities include closing accounts prior to period-end, performing workday assessments to identify potential bottlenecks, implementing a plan for mock close cycle to test remote readiness, and anticipating review logistics and data requirements.
- Consider opportunities to shorten close activities. Some examples include shifting non-key accounts into non-quarter end months, using estimates for accruals, simplifying allocation methodology and approach, implementing new materiality thresholds for non-key account reconciliations, increasing approval limits for close adjustments.
- Standardize templates and enforce procedures to ensure consistency and streamline review cycles
- Re-think ways of working to be remote-friendly
- Pursue additional automation opportunities. Some examples include automating interfaces, allocations, implementing workflow tools

Q81 What measures can be taken by entities to ensure that their internal control over financial reporting are effective during the period impacted by the coronavirus outbreak?

Response

Entities may face challenges during the period impacted by the coronavirus outbreak to establish that their internal control over financial reporting were effective during such times. In such circumstances, entities may need to implement additional controls or make changes to existing controls that are in place. Entities will have to continuously monitor if any of the controls in place may not be effective during the time of lockdown when people are working remotely from home and look for the alternate controls that can be implemented. Also, management will have to make the statutory auditor understand the design of new controls or changes to existing controls for them to perform additional procedures to obtain sufficient appropriate audit evidence that the controls were designed and operating effectively as of the period end.

How we see it

It is recommended that entities make maximum use of regulatory reliefs given by various authorities with respect to timing of filing of the financial results and conduct of board meetings for the approval of the financial statements so that they can give due consideration to the events that have happened on account of the coronavirus outbreak in the past few weeks in preparation of their financial statements. They can also provide appropriate information to users of the financial statements. Also, one of the learning points from this crisis is that entities should focus more on automated controls rather than manual controls to ensure effective operation of finance function during crisis time.

Appendix 1

Summary of key changes to this publication

We have made important changes to this publication since the April 2020 edition, to address evolving issues and expand our discussion of certain topics. The list below summarizes the most significant changes we made in this updated publication.

Section 3 Revenue recognition

- Added Q10 to provide guidance on enforceability of the contracts considering lockdown

Section 4 Financial instruments

- Updated Q22 to include impact of the moratorium on CARO 2020 reporting
- Added Q24 on impact of missed forecasts on ability to designate new hedges

Section 7 Leases

- Added discussion on the collectability considerations of lessors
- Updated response to Q39 and added Q40, Q47, Q48, Q49 and Q50 in light of amendment to IFRS 16 on rent concessions and similar amendment proposed to Ind AS 116

Section 8 Employee benefits

- Added Q57 on appropriateness of using extrapolation technique for quarterly measurement of net defined benefit obligations (assets)

Section 12 Other matters

- Added Q73 on impact on applicability of Ind AS to private companies with listed non-convertible debentures due to proposed amendment

Section 13 Key presentation and disclosure

- Updated discussion to cover illustrative disclosure requirements of SEBI
- Added Q75 on the consideration of the use of alternative performance measures
- Added Q76 on the disclosure impacts due to change in definition of micro, small and medium enterprises

Section 14 Book closure and audit

- Updated discussion to cover further relaxations provided by regulatory authorities

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