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IND AS

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IND AS 21 Effects of Changes in Foreign Exchange Rates

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Foreign currency transactions

- ***Include :***

- Accounting for transactions entered in a foreign currency

- Translation the financial statements of a foreign operation *being a branch, subsidiary, associate or a joint venture* for inclusion in the financial statements of the reporting entity (for consolidation purposes)

- ***Excluded :***

IND AS 21 does not deal with foreign exchange forward contracts and other similar financial instruments that are dealt with by IND AS 109.

*[**AS-11** in addition to deals accounting for foreign currency transactions in the nature of forward exchange contracts]*

Key Terms

- ***Spot exchange rate:***
  - Exchange rate for immediate delivery – also can be referred to as transaction date rate

- ***Closing rate*:**
  - Exchange rate as at balance sheet date

- ***Presentation currency:***
  - The currency in which the financial statements of an entity is presented

- ***Foreign currency:***
  - Is the currency other than the functional currency of an entity and transactions in foreign currency are referred to foreign currency transactions

Key Terms

- ***Foreign operation:***

- ✓ is a subsidiary, associate, joint venture or branch of **the reporting entity** the activities of which are based or conducted in a country or currency other than those of the reporting entity

- ***Net investment in foreign operation*: is**

- ✓ Receivable / payable to the foreign operation;
- ✓ Its settlement is neither planned not likely to occur in the foreseeable future;
- ✓ **includes** long term receivables or loans *but does not include trade receivables or trade payables*
- ✓ **In case of group,** such a net investment in a foreign operation can be that of the parent, or any subsidiary in the group (including another foreign operation)

(Is in the nature of an equity)

- ***Monetary items:***

- ✓ units of currency held and assets or liabilities to be received or paid in fixed or

Functional currency – the key aspects

- Each entity, whether a stand-alone, an entity with foreign operations (parent) or a foreign operation (such as subsidiary or branch) has to determine its functional currency in preparing financial statements;

- Functional currency cannot be by choice, an entity may have financial statements prepared in any currency, i.e. presentation currency can be by choice

- **No group functional currency,** however the presentation currency used in preparing the group financial statements may be the functional currency of the parent

- Functional currency must be consistently applied from period to period

- ***The indicators of the functional currency of an entity:***

a. **Sales:** the currency that mainly influences the sales prices for its goods / services – the currency in which the prices are *denominated and settled* ***and*** the currency of the country whose competitive forces and regulations mainly determine the sales prices of its goods and services

Presentation currency – the key aspects

- ✓ Presentation currency can be any currency – can be a matter of choice

- ✓ **in case of a group,** the presentation currency may be ***but not always*** the functional currency of the parent entity

- ✓ **Change in presentation currency** requires retrospective application.

Functional currency of the foreign operation – additional tests

- The INTENT → To determine whether the functional currency of the foreign operation is the same as that of the reporting entity.

Factor	If YES	If NO
Whether activities of foreign operation are carried out as an extension of the reporting entity, rather than with a significant degree of autonomy	**same** functional currency	**Different** functional currencies
Whether transaction with the reporting entity are a high or low proportion	**same** functional currency	**Different** functional currencies
Whether cash flows of the foreign operation directly impact the cash flows of the reporting entity and are readily available for remittance to it	**same** functional currency	**Different** functional currencies

Functional currency of the foreign operation – additional tests

- THE INTENT → To determine whether the functional currency of the foreign operation is the same as that of the reporting entity.

Indicator	If YES	If NO
Financial independence: Whether cash flows from activities of the foreign operation are sufficient to service existing and normally expected debt obligations without any funds being made available by the reporting entity	**Different** functional currencies	**same** functional currency

Functional currency – Identification

The CASE	The functional currency
X ltd and Indian company prepares its financial statements in Indian Rupees. X Ltd is engaged in the business of exporting automobiles to overseas countries like Brazil, Indonesia, Japan and Malaysia. X Ltd's sales price of automobiles, which are in INR, are largely affected by exchange rate movements of the respective countries. Determine the functional currency of X Ltd as per IND AS 21?	
X Ltd is an insurance BPO service entity and provides services to many international clients. As a strategy to provide best business deliverables, most of the staff of X Ltd are foreign expatriates and their salaries are directly remitted in US$ to their accounts in respective countries . Determine the functional currency of X Ltd?	

Functional currency – Identification

The CASE	The functional currency
X Ltd is in the business of manufacturing and exporting readymade garments and the functional currency of X Ltd is Indian Rupees. It has a branch in the US to which it supplies the readymade garments. The US branch, under a contractual arrangement with X Ltd, is required to sell these only to the customers of X Ltd in the US and remit the proceeds to X ltd? Determine the functional currency of the US branch	
Continuing with the above example(iii), in another scenario, the US branch is under a profit share agreement with X Ltd to sell the readymade garments in the US. Most of the sales are done in the US markets and related expenses are also incurred in its local currency. After retaining the profit share, the balances of the sales proceeds are remitted to X Ltd. Determine the functional currency of the US branch.	

Functional currency- some key aspects

- ***X Ltd is a call centre entity providing services to many international overseas clients. Most of the staff were locally sourced and the cost of salary was settled in Indian Rupees. However due to rapid technological changes and requirements from overseas clients, X Ltd appointed foreign experts and their salary payments were directly settled in US$. Hence significant labor costs were denominated and settled in US$. Hence in accordance with Para 9(b) the new functional currency of X Ltd is now US$ on the date of change i.e.31.12.2015***

- ***X Ltd converted the financial statements for the period 1.4.2015 to 31.12.2015 into the new functional currency retrospectively from 1.4.2015 by using the average exchange rate for the period US$1 = INR 45.The exchange rate as on 31.12.2015 is US$1 = INR 50***

Whether X Ltd is allowed to change its functional currency from INR to US$	

- ✓ ***a***

Functional currency- some key aspects

Whether X Ltd should adopt change its functional currency from INR to US$ retrospectively?	
If the functional currency of X Ltd is changed from INR to the USD, whether the presentation currency of X Ltd will also become US$?	
In the prior period, X Ltd had recognized the exchange differences arising from translation of the US branch to the presentation currency of X Ltd in the other comprehensive income and recognized the same in equity. On the date of change in the functional currency, if possible, whether X Ltd should reclassify such amounts recognized in OCI in respect translation of financial statements of the US branch to profit and loss?	

Conversion – Foreign Currency transactions

- **The applicable exchange rates**

	The foreign currency item	Applicable exchange rate for translation into functional currency
1	All foreign currency transaction items – **INITIAL RECOGNITION** (*whether monetary or non monetary)*	At **SPOT exchange** rate between the functional currency and foreign currency on the date of transaction
2	**SUBSEQUENT REPORTING PERIODS**	
A	**All Monetary items**	**Closing rate** – rate on reporting date
B	**Non Monetary items**	
	Carried at Historical cost	Exchange rate at transaction date
	Carried at Fair Value	Exchange rate when fair value was measured
C	**Equity and Incomes / Expenses**	Transaction date rate

Conversion – Foreign currency transactions

- **The applicable exchange rates**

	The foreign currency item	Applicable exchange rate for translation into functional currency
3	**Non monetary item whose carrying amount is determined by comparing two amounts:** *for example* a. **Inventory** (cost or NRV); or b. **Non monetary asset** being tested for impairment (carrying amount or recoverable amount	**For cost or carrying amount** Apply transaction date exchange rate **For NRV or recoverable amount** Apply exchange rate on the date the fair value is determined (which is generally the closing date)

Conversion – Foreign currency transactions

- **Exchange Gain or loss**

	The foreign currency item	Reason for exchange difference	RECOGNISED IN
1	**All monetary items**	**EITHER** a. Settlement of monetary items; or b. Difference between, transaction date and closing date rates; **OR** current and previous closing rates	**Profit and loss account** **[**either in the same period (if settled in the same period) OR in each period upto date of settlement (if settled in subsequent period)**]**
2	**Non monetary item**	**In case of upward / downward revaluation** Difference between historical rate and rate at revaluation date	***When gain or loss on a non monetary item is recognized in OCI (e.g. IND AS 16 - revaluation of property plant and equipment), any exchange component of that gain or loss is also recognized in OCI. Conversely when gain /loss on a non monetary item is recognized in P/L any exchange component of that gain / loss is also recognized in P/L.***

Conversion – Foreign currency transactions

- **Exchange Gain or loss**

	The foreign currency item	Reason for exchange difference	RECOGNISED IN
3	**Monetary items – reporting entity's Net Investment in a Foreign Operation**	**Difference either due to transaction and closing date rates OR between two closing date rates**	In the **separate** financial statements of the reporting entity or the individual financial statements of the foreign operation **Profit and loss account**
			In the **consolidated** financial statements (the reporting entity and foreign operation) **In other comprehensive income**

Translation – TO the presentation currency (from functional currency

❖ **The applicable exchange rates and exchange gain / loss**

	Particulars	Functional currency is currency of Non hyperinflationary economy	Functional currency is currency of hyperinflationary economy
1	**All assets and liabilities** for each balance sheet presented – monetary & non Monetary (including comparatives)	**Closing rate**	**Closing rate**
2	**Equity**	**Exchange rate at transaction date**	**Closing rate**
3	**Incomes and expenses** for each profit and loss statement presented (including comparatives)	**Exchange rate at transaction date**	**Closing rate**

Translation – TO the presentation currency (from functional currency

- **Exchange Gain or loss**

	Particulars	Reason for exchange difference	RECOGNISED IN
1	**All items of assets, liabilities, incomes and expenses**	**EITHER** a. Translating incomes and expenses at transaction date rates and assets and liabilities at closing rates ; b. Difference between current and previous closing date rates	**Other comprehensive income** (in both cases whether or not functional currency is the currency of an hyperinflationary economy)
2	**Exchange differences relate to a foreign operation that is consolidated but not wholly owned and attributable to *non controlling interests***		**As part of NCI** in the consolidated balance sheet

Disposal / Partial Disposal – Foreign Operation

- Disposal of a foreign operation may either occur through sale, liquidation, repayment of share capital, or abandonment of all or part of that entity.

Disposals are categorised as

DISPOSAL

PARTIAL disposals

- **Reclassification:** Exchange gains / loss recognised in other comprehensive income is *reclassified from equity to profit and loss* when on the date the gain or loss on the disposal is recognised

Disposal / Partial Disposal – Foreign Operation

• Disposal

- ✓ is disposal of entire interest in a foreign operation;
- ✓ **Includes**: in case the foreign operation is

<u>A subsidiary -></u> partial disposal leading to loss of control:

<u>An associate / JV -></u> partial disposal which leads to loss of significant influence or loss of joint control making the investment a

• PARTIAL Disposal

- ✓ IS any reduction in the entity's ownership in the foreign operation
- ✓ Any **write down** of carrying amount of foreign operation due to impairment losses or others *is not partial disposal* and on such write down no amount of exchange gain/loss recognised in OCI is reclassified to profit and loss

Foreign Operation being →	Wholly owned subsidiary	NOT wholly owned subsidiary	Others - associate / JV / Branch
Disposal	Entire exchange differences reclassified to P&L	Exchange differences attributable to NCI **shall be derecognised – not reclassifed**	Entire exchange differences reclassified to P&L
PARTIAL disposal	Recognise proportionate share of cumm. exchange diff in OCI to NCI	Re-attribute proportionate share of cumm exchange diff in OCI to NCI	Reclassify proportionate share to P&L

IND AS 23 Borrowing Costs

Borrowing costs

- ***Include :***
  - Interest expense calculated using *effective interest rate method* (as described in IND AS 109);
  - Finance charges in respect of finance leases (IND AS 17);
  - Exchange difference arising from foreign currency borrowings to the extent they are regarded as adjustment to interest costs Para 6(e)

- **Does not apply to borrowing costs** directly attributable to the acquisition, construction or production of:
  - A qualifying asset measured at *fair value* eg. biological asset (IND AS 41); OR
  - **Inventories** that are manufactured or otherwise produced in large quantities on a repetitive basis

Qualifying Assets

- A qualifying assets is one that necessarily takes a substantial period of time to get ready for its intended use or sale.
- ✓ Inventories
- ✓ Manufacturing plants
- ✓ Power generation facilities
- ✓ Intangible assets
- ✓ Investment properties
- ✓ Bearer plants

- ***Qualifying assets do not include :***
- ✓ Financial assets;
- ✓ Inventories manufactured / produced over a short period of time
- ✓ Assets that are ready for their intended use or sale when acquired

Recognition of borrowing costs in the financial statements

- **Borrowing costs directly attributable to the acquisition, construction or production of a qualifying asset**

Are capitalised as part of the cost of the asset

- O

Are recognised as expense in the period in which incurred

Example 1

- ***1.4.2014 A Ltd purchased land for construction of office building & cost of construction expected –Rs 50 lacs***

construction process commenced and expenses incurred for plan approvals, architect fees etc.

A Ltd approached ABC bank for a loan of Rs 30 lacs at 10% interest per annum. The loan was sanctioned on 30.06.2014 and interest was payable thereafter every month at the end of each month.

All the pre-construction formalities were completed by the end of December 2014 and on 31.12.2014, A Ltd received the final order approving the construction plan. The construction of the office building commenced on 15.01.2015

The borrowing costs incurred for the period from 31.07.2014 to 31.03.2015 (assuming no principal repayment has commenced to date) was Rs 225000 and entire borrowing costs for the period was capitalised. Auditors allowed capitalisation of the borrowing costs only for the period from 15.01.2015 to 31.3.2015 . Whether they are correct in doing so?

Would your answer be different if A Ltd, after acquiring the land on 1.4.2014,

Capitalisation of borrowing costs

When do you COMMENCE capiatlisation	When do you SUSPEND capitalisation	When do you CEASE capitalisation
*From the date when the entity **first** meets all the following conditions:* ✓ it incurs expenditures for the asset; ✓ it incurs borrowing costs; AND ✓ it undertakes activities that are necessary to prepare the asset for its intended use or sale	During extended periods in which it suspends active development of a qualifying asset NO suspension of capitalisation *:* ✓ *during* period when the entity carries out substantial technical and administrative work; OR ✓ temporary delay is a necessary part of the process of getting an asset ready for its intended use or sale	*When* substantially all activities necessary to prepare the qualifying asset for its intended use or sale **is *complete*** ***What to ignore*** ✓ continuance of routine administrative work ✓ outstanding minor modifications ***e.g.*** decoration of property to purchaser's or user's modification

Example 1

Answer:

- ***(a)*** In the given case, the charge on account of borrowing costs commences on 30.07.2014 i.e. the date on which the first payment towards interest cost is made. On this date X Ltd has already undertaken activities related to the construction of the office building and has also incurred expenses for the same.

Hence the capitalization of the borrowing costs should commence from the date of payment of the first interest cost i.e. 31.07.2014 and not from 15.01.2015 when the actual construction activity commences

- ***(b)*** As mentioned earlier that commencement of capitalization of borrowing costs commences when the entity commences activities related to construction necessary to prepare the asset for its intended use or sale, incurs expenditures for the asset and also incurs borrowing costs. *However borrowing costs incurred* while land acquired for building purposes *is held*

Example 2

(a) ***X Ltd is constructing an office building and is already incurring borrowing costs for the same. However as per the construction regulations, the construction plans are only approved floor wise and after constructing three floors, permissions are again required to be made to the regulatory authorities which take around 3-4 months to get the same. X Ltd however continues to incur borrowing costs during this period when no construction activity is being carried on. Please advise whether X Ltd can capitalize the borrowing costs incurred during this period when the construction activity is temporarily suspended?***

(b) Assume that in the given example, the construction of the office building is completed on 30.12.2014. Decorations to the office building viz. putting imported venetian blinds, decorating a portion of walls for display purposes, are still in progress. Can borrowing costs incurred during the progress of such works be a part of the cost of the office building i.e. whether they can be capitalized.

(c) Would your answer be different if the construction of the office building is complete but administrative work relating to getting permissions to occupy the premises, getting water and electricity connections are still pending?

Capitalisation of borrowing costs

When do you COMMENCE capiatlisation	When do you SUSPEND capitalisation	When do you CEASE capitalisation
*From the date when the entity **first** meets all the following conditions:* ✓ it incurs expenditures for the asset; ✓ it incurs borrowing costs; AND ✓ it undertakes activities that are necessary to prepare the asset for its intended use or sale	During extended periods in which it suspends active development of a qualifying asset NO suspension of capitalisation *:* ✓ *during* period when the entity carries out substantial technical and administrative work; OR ✓ temporary delay is a necessary part of the process of getting an asset ready for its intended use or sale	*When* substantially all activities necessary to prepare the qualifying asset for its intended use or sale **is *complete*** ***What to ignore*** ✓ continuance of routine administrative work ✓ outstanding minor modifications ***e.g.*** decoration of property to purchaser's or user's modification

Example 2

Answer

(a) During an extended period when the active development of a qualifying asset is suspended, borrowing costs incurred during such periods are not eligible for capitalization as the standard treats such borrowing costs as costs for holding partially completed assets. However where the temporary suspension is an unavoidable process of getting an asset ready for its intended use or sale (i.e. the construction of the asset), then the standard allows capitalization of such borrowing costs as such a temporary suspension of the construction activity is a necessary part of the entire construction process. **Hence X Ltd can capitalize borrowing costs** incurred during the periods when the construction activity is suspended due to the permissions obtained floor wise.

(b) Cessation of capitalization of borrowing costs is when the substantially all activities necessary to prepare the qualifying asset for its intended use or sale is *complete* even if routine administrative work may still continue or minor modifications to the asset as per user specifications are still pending. Hence decorations to the office building viz. putting imported venetian blinds, decorating a portion of walls for display purposes still indicate that substantially all activities to the construction of the office building are complete and therefore **borrowing costs incurred after 30.12.2015 when**

Measurement of borrowing costs

Specific borrowings

General borrowings

[redacted]

[redacted]

- General borrowings refer to borrowing of funds where the financing activities are centrally coordinated within an enterprise and the

IND AS 27 Separate Financial Statements

Key aspects of the standard

- **Separate financial statements** are those presented **(i)** by a parent (i.e. an investor with control of a subsidiary) or **(ii) by** an investor with joint control of, or significant influence over, an investee

- Financial statements that do not have an investment in subsidiary, associates or joint ventures are NOT separate financial statements

- **Consolidated financial statements** are financial statements presented for a group or financial statements in which investments in associates or joint ventures are accounted for using the *equity method*

- An entity exempted by IND AS 110 *Consolidated financial statements* OR by IND AS 28 *Accounting for Investments in Associates or Joint Ventures* may present its separate financial statements as its only financial statements – *similar is the case of an investment entity*

Key aspects of the standard

- **Investments in subsidiaries, associates or joint ventures are** presented in the entity's separate financial statements either at

a) **Cost**: OR

b) **In accordance with IND AS 109**

- **For similar class of investments –** same accounting to be applied

- **Investor or a Parent being an Investment entity:** when these entities opt to measure its investments in accordance with IND AS 109 at FVTPL (in its consolidated financial statements), they shall also account for its investments in the *same manner* in its separate financial statements

- **Investments when they are classified as held for sale:**

- ✓ **If they were initially carried at cost:** measure in accordance with IND AS 105 ; OR

Accounting for Subsidiary – Parent, becoming, or ceasing to be, an investment entity

- **The Parent becoming an investment entity**

<table>
<tr><th>Carrying amount BEFORE date of change</th><th>Subsequent carrying amount (on date of change)</th><th>Accounting for differences in fair value</th></tr>
<tr><td rowspan="3">Either at COST or in accordance with IND AS 109</td><td rowspan="3">At
Fair Value through Profit and loss</td><td>Recognised in
Profit and loss</td></tr>
<tr><td>Cumulative amount recognised in relation to subsidiaries in the OCI</td></tr>
<tr><td>Shall be reclassified to Profit and loss on date of change of status
(as if the investment entity had disposed off those subsidiaries)</td></tr>
</table>

Accounting for Subsidiary – Parent, becoming, or ceasing to be, an investment entity

- **The Parent Ceasing to be an investment entity**

Carrying amount BEFORE date of change	Subsequent carrying amount (on date of change)	Accounting for differences in fair value
At Fair Value through Profit and loss	**Either at** ***(a) COST*** (fair value of the investment on date of change of status to be the deemed cost); OR ***(b) Continue to account for the investment in accordance with IND AS 109***	NIL