

Query No. 18

Subject: *Accounting for financial restructuring of an aviation company.*¹

A. Facts of the Case

1. An aviation company (hereinafter referred to as ‘the Company’) is 100% owned by the Government of India (GoI). The Aviation industry in India has been facing many challenges in the form of volatile fuel prices with high component of sales tax by various states Governments, loss of pricing power as fares were not determined on cost plus basis. The Company was also affected by these issues as a result of which, it has been making consistent losses since merger. Interest on aircraft loans on newly acquired aircraft and on working capital due to accumulated losses besides depreciation of the Indian Rupee vis-a-vis the USD also affected its profitability besides merger issues. In the airline industry nearly 70% of costs are dollar denominated.

2. The Government of India (GoI) approved the Turn Around Plan/Financial Restructuring Plan in the year April 2012 to bring about operational and financial efficiencies with a view to make the Company a leader in Indian aviation, deliver a high quality of service and be the epitome of Indian hospitality. Subsequently, the GoI infused nearly INR 32,000 crores as equity into the Company at various stages between 2012 and 2018 for which equity shares were allotted to the GoI.

3. However, despite the infusion of capital, the Company continued to make losses, due to the various challenges faced internally and in the aviation industry. At a meeting held on September 7, 2018, under the Chairmanship of the then Finance Minister to discuss the plan for operational and financial efficiency, immediate measures in the form of financial support, monetizing on non-productive assets of the Company, transfer of certain specified debts of the Company to Special Purpose Vehicle (SPV) to reduce the servicing liability were taken with a view to achieve an operational/financial turnaround (Minutes of the meeting dated September 07, 2018 to discuss the plan for operational and financial efficiency in the Company has been supplied separately by the querist). The SPV is 100% owned by GoI. In line with the above, Company’s specific Alternate Mechanism (AISAM) comprising of a Group of Ministers, had at the same meeting, decided that the debt of the Company from various banks amounting to INR 29,464 crores would be transferred to SPV w.e.f. October 1, 2018 along with the non-core assets of the Company including, inter-alia, arts, artifacts and subsidiaries (in the form of shareholding of subsidiary companies). The balance debt of INR 28,701 crores and current liability would be retained in the Company. The loan identified for transfer to SPV mainly comprised loans under the Financial Restructuring Plan (FRP), raised from 19 banks and aircraft loans raised from financial institutions for aircraft acquisition. However, due to the issues relating to the transfer of debt by banks to SPV and the reluctance of banks to agree to this, it was decided subsequently that the debt of INR 22,064 crores would be repaid by raising the monies through issue of the Government Guaranteed Bonds in the SPV and these monies will be given to the Company to repay the loans and the balance amount of INR 7,400 crores as Non-Convertible Debentures (NCDs) would be transferred from the Company’s books of account to SPV as an existing debt.

4. The SPV, which was formed as a public limited company under the Companies Act, 2013 and, is wholly owned by the GoI to which the debt was proposed to be transferred, raised money to the extent of INR 22,064 crores through issue of GoI guaranteed bonds, in three tranches, has transferred the monies to the Company to repay the ‘Financial Restructuring Plan’ (FRP) debts of

¹ Opinion finalised by the Committee on 27.8.2020.

the Company as well as certain aircraft loan. Subsequently loans equal to this amount has got repaid as of date. The novation of debt of INR 7,400 crores from the Company to SPV is under process.

5. GoI will service the debt of SPV through adequate provision in the form of budgetary support every year in the Annual Finance Budget as well as in Supplementary Demand for Grants (Extract from the budget booklet of the Ministry of Civil Aviation has been supplied separately by the querist). The proceeds (effective from October 1, 2018) from monetization of assets transferred from the Company as well as the money realised from the sale of subsidiary companies and other non-core assets would also be used to service the liability on the bonds by the SPV. An Escrow mechanism has been put in place for this purpose both in the Company as well as in the SPV to separately capture the proceeds of the monetization and other sale proceeds. However, there would be a gap in the fair market value of non-core assets including monetization of immovable properties and subsidiaries transferred to SPV and the debt assumed by the SPV from the Company. For the purpose of the Opinion, it is assumed that the fair market value (FMV) of the assets transferred from the Company over a period of time to the SPV would be around INR 12,000 crores and the debt assumed by the SPV is INR 29,464 crores and hence there will be a gap of INR 17,464 crores approximately between liability assumed by SPV and debt transferred to SPV. GoI is in the process of divesting the entire equity in the Company and the assignment of doing so has been entrusted to a Transaction Advisor. Government is therefore, likely to clean up the balance sheet of the Company in order to make it saleable.

6. The querist has provided a brief summary of the facts of the query as follows:

- (i) The Company and the SPV are companies wholly owned by the GoI. According to the divestment programme and the instructions from GoI, the SPV has raised monies of Rs. 22,064 crores through the issue of bonds in its name. The payment of interest and principal of these bonds is fully guaranteed by the Govt. of India. The entire amount raised by the SPV has been transferred to the Company and from these proceeds, the Company has paid off its debt of equal amount against aircraft/working capital loans etc. Also, the SPV also assumed its debt in the form of NCDs of Rs. 7,400 crores issued to LIC and EPFO. Consequently, the Company will be able to reduce its debt to the extent of Rs. 29,464 crores. (Minutes of the meeting dated May 30, 2019 with budget division of Department of Economic Affairs, Ministry of Finance regarding discussion on proposed funds raising for refinancing of debt of INR 29,464 crores has been supplied separately by the querist). The Company does not have any obligation to repay this debt to the SPV as the entire servicing of this debt both in terms of principal as well as interest payment is to be done by Govt. of India Budgetary Support (also refer paragraph 9 below).

The NCDs of Rs. 7,400 crores are novated to the SPV. The Company is legally released from the obligation towards the NCD holders as after the novation of these NCDs to the SPV, all liabilities relating to these NCDs will be transferred to the SPV. (Also refer paragraph 9 below)

- (ii) On the other hand, the Company will transfer the proceeds of immovable properties and investments in identified subsidiaries at cost without any additional consideration to the SPV. Any receivables / payables from these identified subsidiaries are to be transferred at book value to SPV. Once these assets are transferred to the SPV, the Company will have no recourse to these assets as they would be the sole properties/assets of the SPV only.

- (iii) The combined value of the above i.e. proceeds from properties sold and cost of investment in subsidiary companies transferred is estimated to be Rs. 12,000 crores.
- (iv) The immovable properties are to be sold over a period of time stretching from Financial Year (F.Y.) 2018-2019 to F.Y. 2020-2021 or even later.
- (v) The Company has no further obligation to repay the shortfall, estimated to be in the vicinity of INR 17,464 crores.
- (vi) The SPV has been formed as part of the divestment process and is owned 100 % by GoI.
- (vii) The transfer of proceeds from immovable properties and transfer of investments in identified subsidiaries from the Company to the SPV has been agreed by Boards of both the companies as per the framework agreement (Framework Agreement approved by the Boards of the Company and the SPV) entered into between the companies for divestment.
- (viii) In the instant case, GoI has provided the assistance, through the SPV as part of the disinvestment program. In the past also, it has provided similar financial assistances to the Company wherein the Company had issued fresh equity shares to the GoI against the financial assistance.
- (ix) In the instant case, there is no requirement to issue any equity shares nor any obligation to repay the amount received as financial assistance from the SPV owned by the GoI.
- (x) The amount of INR 22,064 crores received by the Company from the SPV in September to October, 2019 has been used by the Company to repay its debt to the banks and financial institutions.
- (xi) The debt assumed by the SPV will be serviced by the Government (interest and principal obligations) by making suitable budgetary provisions in the Finance Budget of the respective years.
- (xii) In F.Y. 2018-19, the Company has classified all the assets, properties, investments which are proposed to be sold/transferred to the SPV under 'Assets held for Sale' in its financial statements.

The above transactions were pending as on October 1, 2018 and are expected to be completed in F.Y. 2019-20 and in F.Y. 2020-21.

7. Terms of Framework Agreement between the Company and the SPV are as follows:

- (i) The Company and the SPV agree that SPV shall transfer the amount to the Company and undertake the obligation for payment to be made pursuant to the Bonds, by execution of all necessary Debt Transfer Documents within reasonable timelines, as mutually agreed between the Parties ("Debt Transfer"). (Clause 2.1)
- (ii) The Parties agree that the Company shall, transfer the Assets to the SPV, by execution of all necessary Asset Transfer Documents, within reasonable timelines as mutually agreed between the Parties ("Asset Transfer"). The Company agrees and acknowledged that it shall have no recourse to the Assets transferred by the Company to the SPV. (Clause 2.2)
- (iii) The Parties agree and acknowledge that for any asset that is not immediately transferred by the Company to the SPV, the Company shall set up a suitable escrow mechanism, as agreed between Parties for deposit of any monies received from such asset and transfer of such monies to the SPV, including any proceeds received from

- disposal or monetisation of such asset by the Company, on the instructions of the SPV. (Clause 2.3)
- (iv) The Parties agree that the ‘Asset Transfer’ and ‘Debt Transfer’ may be undertaken in multiple tranches. (Clause 2.4)
 - (v) The Parties agree that as pursuant to discharge of their mutual obligations as envisaged, that for the Debt Transfer of INR 29,464 crores from the Company to the SPV, which shall be reflected in the books of the SPV as debt, the GoI through the SPV shall provide the Company an amount of a capital grant to the extent of shortfall post monetisation of non-core assets of the Company (as and when such non-core assets including transfer of subsidiaries and other assets is implemented), the proceeds of which shall be forthwith utilised for reduction in the debt transferred to the SPV. (Clause 2.5)
 - (vi) The Parties hereby agree that the [assignment/novation] of Bonds to the SPV thereof shall be deemed to be effective from the Effective Date i.e. October 1, 2018 and upon [assignment/novation] of Bonds to the SPV, the SPV shall assume all rights, obligations and liabilities in relation to such Bonds, on and from the Effective Date. It is hereby clarified that all interest, default interest, liquidated damages, fees, commissions, expenses and all other charges or amounts payable to the holders of the Bonds (and their respective agents and trustees) in respect thereof shall be to the account of the SPV and any such amount paid by the Company on behalf of the SPV on and from the Effective Date, shall be reimbursed or paid to the Company by the SPV on such terms and in a manner as may be agreed between the Parties from time to time. (Clause 2.6)
 - (vii) The Parties hereby agree that the payment of the amounts by the SPV to the Company, thereof was intended from the Effective Date i.e. October 1, 2018 for the Company to discharge its debt to the extent of the Amounts (“Debt”). To effectuate the understanding between the Parties, the SPV agrees and undertake that the SPV shall be deemed to have assumed the obligations in relation to the Debt and all interest, default interest, liquidated damages, fees, commissions, expenses and all other charges or amounts payable to the lenders of the Company in relation to the Debt (and their respective agents and trustees) in respect thereof shall be to the account of the SPV, on and from the Effective Date, shall be reimbursed or paid to the Company by the SPV on such terms and in a manner as may be agreed between the Parties from time to time. (Clause 2.7)

8. *Accounting treatment proposed by the Company:*

The SPV has been formed as part of the divestment process and is owned 100% by the GoI. Also, the above transaction of transfer of proceeds from immovable properties and transfer of investments in identified subsidiaries has been agreed as part of the framework agreement for divestment approved by the GoI. Hence, it can be interpreted that SPV is acting on behalf of the GoI and as such, the contributions can be considered to be made by the GoI itself, albeit through a company owned 100% by itself. Hence, in substance, the financial assistance is in the nature of an equity contribution from the GoI and it would be appropriate to recognise such amount directly in ‘capital reserve’ under the head ‘other equity’. On the above grounds, the following accounting treatment is proposed to be adopted by the Company in the financial year 2019-20:

- a. On novation of the NCDs of INR 7,400 crores to SPV, the NCD debt would be derecognised at carrying amount by crediting ‘capital reserve’ under the head ‘other equity’.

- b. On receiving cash of INR 22,064 crores from SPV,
 - (i) The Company will record a financial liability i.e. payable to SPV, to the extent of INR 12,000 crores (estimated proceeds of non-core assets at fair value and investment /receivable/payables at book value) since there is a liability to repay amounts to SPV and
 - (ii) the balance amount of INR 10,064 crores will be recorded as 'capital reserve' under the head 'other equity' in F.Y. 2019-20;
 - c. The liability of INR 12,000 crores will be reduced as and when payment of proceeds of immovable property or transfer of investments/assets takes place to the SPV. On repayment of the entire amount payable to SPV in future years, if there is some excess or shortfall, the same will be debited or credited to other equity.
 - d. The difference between written down value of identified non-core assets and the sale proceeds/fair value of those non-core assets will be taken to the statement of profit and loss.
 - e. Investments in identified subsidiaries and receivables/payables pertaining to these subsidiaries are transferred at cost as per framework agreement and not at fair value. Accordingly, the company does not envisage any impact on statement of profit & loss or capital reserve on account of fair value of these subsidiaries.
9. The querist has separately informed as follows:
- (a) Framework Agreement (a copy of the same provided by the querist for perusal of the Committee) is yet to be signed. The copy supplied is the final draft of the framework agreement which has been approved by the respective Board of Directors of the Company as well as the SPV. The same is complete in all respects and may be treated as final.
 - (b) As regards, the novation of bonds of Rs 7,400 crores to SPV by the Company, the process for the same is still on. The major holders of the bonds namely LIC and Coal Mines PF Trust have already given their concurrence and No Objection for the novation of these bonds to SPV. Further, it may also be noted that when the Company had issued these bonds in its books, the same were fully guaranteed by Govt. of India. In fact, for the novation of these bonds to SPV, the Government has again issued its Letter of Assurance, assuring the payment of both principal as well as interest and meeting these obligations from the Government Budgetary Support. (The Letter issued in this regard by GoI, Ministry of Finance has been provided separately by the querist for the perusal of the Committee)
 - (c) Further, it is also confirmed that post the transfer of the entire debt of Rs 29,464 crores (out of which Rs. 22,064 crores has already been effected before 31st March, 2020) from the books of the Company to SPV, the Company will be fully discharged/legally absolved of all the liabilities relating to this debt, which will then be the responsibility of SPV, which in turn stands fully guaranteed by the Government of India.
 - (d) Clause 2.5 of the Framework Agreement clarifies the treatment to be afforded to the net shortfall/excess that will exist in the books of the Company and the SPV after the entire transaction is over and all inter adjustments of loan transfers as well as transfer and sale of other non-core assets and liabilities from the Company to the SPV have been completed. This net shortfall/excess was proposed to be made good by means of a Capital Grant from GoI through the SPV to the Company.

- (e) Further, the querist has informed that there are timing differences in executing the various parts of the transaction (which may spread over more than one financial year) and the value of the transaction of sale cannot be predicted with certainty. Clause 2.5 of the Framework Agreement is included to ensure that there is no liability on the part of the Company to make good or recoup any difference between the loans taken over and the assets transferred. At the appropriate time, when the transaction is completed, the difference will be treated as Capital Grant.

B. Query

10. Considering the above background, the querist has sought the opinion of the Expert Advisory Committee on the following issues:

- (i) Whether the proposed accounting treatment mentioned in paragraph 8 above is correct.
- (ii) If the accounting treatment proposed above is incorrect, whether the above Government supports through SPV can be treated as ‘Government Grant’ under Ind AS 20, ‘Accounting for Government Grants and Disclosure of Government Assistance’, as in substance, the GoI is making a grant to the Company but routing it through the SPV and the entire amount be credited to ‘statement of profit and loss’ in F.Y. 2019-20 itself instead of ‘other equity’, for the differential amount of INR 17,464 crores (INR 7,400 crores NCDs + INR 22,064 crores other debt – INR 12,000 crores being estimated proceeds of the assets/investments to be transferred) being the debt to be extinguished by the SPV.
- (iii) If the answer to query (i) is in negative and the answer to query (ii) is also in negative, the Company proposes to treat the difference amount, as cessation of liability and write back the amount to the Statement of Profit & Loss. Whether this treatment would be in order.

C. Points Considered by the Committee

11. The Committee notes that the basic issue raised by the querist relates to the accounting treatment in the separate financial statements of the Company in respect of the above-mentioned proposed financial restructuring plan of the Company comprising of transfer of assets (including investment in subsidiaries), transfer of debts/liabilities and the funds received from the GoI through its 100% owned SPV, in the context of Indian Accounting Standards (Ind ASs), notified under the Companies (Indian Accounting Standards) Rules, 2015 (hereinafter referred to as ‘the Rules’) in the separate financial statements of the Company. The Committee has, therefore, considered only this issue and has not examined any other issue that may arise from the Facts of the Case, such as, whether or not the SPV and the Company are controlled by the Government of India, accounting in the consolidated financial statements of the Company, classification of the non-core assets as non-current assets held for sale/disposal/distribution or as discontinued operation under Ind AS 105, impairment of the non-core assets, accounting for prior period errors under Ind AS 8, related party disclosures under Ind AS 24, accounting treatment in the financial statements of the SPV, appropriateness or otherwise of the going concern assumption of the Company/ the SPV, accounting before the Framework Agreement becomes legally effective, timing of legal release of the liabilities for the Company, accounting for any income or expense accrued on the assets/liabilities being transferred as part of financial restructuring (such as, dividends received from subsidiaries, interest paid for servicing the bonds, etc.) etc. Further, the Committee wishes to point out that the opinion expressed hereinafter is in the context of Indian Accounting Standards as applicable for the financial year 2019-20, though the timing of the accounting treatment

discussed hereinafter will depend on the period/year in which the compliance with the requirements of the relevant Ind AS, as detailed below, will be made. The Committee has restricted the opinion only to the accounting issues under Indian Accounting Standards and not looked into the legal or taxation or financial management issues arising from the facts submitted by the querist. Furthermore, the opinion expressed hereinafter lays down the principles to be followed while accounting for the transactions as part of financial restructuring without commenting on various figures or values of financial liabilities, assets, etc.

At the outset, the Committee notes from the facts in the extant case and various documents supplied by the querist that the Framework Agreement referred to by the querist although approved by the Board of Directors of both the Company and SPV, but is yet to be duly signed by the parties concerned; however since the querist has asserted that the same may be considered as the final, the Committee has proceeded on the same premise. Similarly, in respect of novation of debt (NCDs) of Rs. 7400 crores, although 'in-principle' NOC has been received from the creditors (viz., LIC, Coal Mines Provident Fund Trust, etc.) and the Ministry of Finance (MoF), Government has also provided its assurance of servicing of principal and interest of the bonds, novation deed is yet to be entered into between the concerned entities. Accordingly, the Committee presumes that there is no uncertainty as far as legal release from the primary responsibility for the liability by the creditor in respect of NCDs and that on Framework becoming legally effective, the novation of NCDs shall also be legally effective, resulting into legal release/transfer for the company from the primary responsibility for its financial liabilities and also the transfer of its non-core assets. It is also noted that asset transfer agreement is also yet to be undertaken, however, based on the facts of the case, it is presumed that there is no uncertainty of occurrence of the transfer and that the transfer is a legal obligation on the Company, once the Framework Agreement becoming legally effective. The Committee has not looked into the legal aspects of the Framework Agreement or the Transfer agreements, or their effectiveness, and has, therefore, assumed, based on the facts provided, that the agreements furnished by the querist are legally binding on the Company, the SPV and the GoI. In this context, the Committee also wishes to point out that if there is change or deviation in any of premise/presumption aforesaid or terms of the Framework Agreement in the current form, the opinion may not hold good.

12. The Committee notes the accounting treatment as proposed by the querist in F.Y. 2019-20:

- On novation of the NCDs of INR 7,400 crores to SPV, the NCD debt would be derecognised at carrying amount by crediting 'capital reserve' under the head 'other equity'.
- On receiving cash of INR 22,064 crores from SPV,
 - The Company will record a financial liability i.e. payable to SPV, to the extent of INR 12,000 crores (estimated proceeds of non-core assets at fair value and investment /receivable/payables at book value) since there is a liability to repay amounts to SPV and
 - the balance amount of INR 10,064 crores will be recorded as 'capital reserve' under the head 'other equity' in FY 2019-20;
- The liability of INR 12,000 crores will be reduced as and when payment of proceeds of immoveable property or transfer of investments/assets takes place to the SPV. On repayment of the entire amount payable to SPV in future years, if there is some excess or shortfall, the same will be debited or credited to other equity.

13. The Committee notes that the GoI is in the process of carrying out the financial restructuring of the Company with the aim to divest its stake in the Company. The Government is therefore, taking steps to make it saleable. For this purpose, the GoI, the Company and the SPV have finalised a Framework Agreement, which is yet to be signed. The opinion sought is in relation to two critical provisions of this Framework Agreement, viz., restructuring of the liabilities of the Company and disposal of the non-core assets, comprising financial assets as well as non-financial assets.

14. In the above context of restructuring, the Committee notes that paragraph 13 of Ind AS 27, 'Separate Financial Statements' makes a reference to group restructuring as follows:

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

- (a) the new parent obtains control of the original parent by issuing equity instruments in exchange for existing equity instruments of the original parent;
- (b) the assets and liabilities of the new group and the original group are the same immediately before and after the reorganisation; and
- (c) the owners of the original parent before the reorganisation have the same absolute and relative interests in the net assets of the original group and the new group immediately before and after the reorganisation,

and the new parent accounts for its investment in the original parent in accordance with paragraph 10(a) in its separate financial statements, the new parent shall measure cost at the carrying amount of its share of the equity items shown in the separate financial statements of the original parent at the date of the reorganisation.”

The Committee notes that the above requirements are not applicable for accounting in the books of the subsidiary, i.e., the Company.

15. The GoI, through the SPV has provided funds of Rs. 22,064 crores to the Company for the purpose of discharging its liabilities of Rs. 22,064 crores comprising of loans from banks. Further, the SPV has also taken over the Company's liability towards its NCDs of Rs. 7400 crores by novation of the NCDs. Also, pursuant to the Framework Agreement, the Company shall be transferring its certain non-core assets comprising the investments in identified subsidiaries and also sale proceeds of certain identified immovable properties to the SPV. Pursuant to above, the GoI through the SPV shall provide the Company an amount of capital grant to the extent of shortfall post monetisation of non-core assets of the Company. This is to ensure there is no liability on the part of the Company to make good or recoup any difference between the loans taken over and the assets transferred.

The Committee further notes that the Company's liabilities in the form of NCDs and loans/credit facilities from banks are in the nature of financial liabilities as defined in Ind AS 32, 'Financial Instruments: Presentation' and are subject to accounting requirements of Ind AS 109, 'Financial Instruments'. In the context of the query relating to the transfer of the Company's liabilities in the form of NCDs to the SPV and financial liabilities due to SPV arising from infusion of Rs. 22,064 crores (utilised for repayment of loans taken from banks), the Committee notes the following requirements of Indian Accounting Standard (Ind AS) 109, 'Financial Instruments':

“3.3. Derecognition of financial liabilities

3.3.1 An entity shall remove a financial liability (or a part of a financial liability) from its balance sheet when, and only when, it is extinguished— ie when the obligation specified in the contract is discharged or cancelled or expires.”

“3.3.3 The difference between the carrying amount of a financial liability (or part of a financial liability) extinguished or transferred to another party and the consideration paid, including any non-cash assets transferred or liabilities assumed, shall be recognised in profit or loss.”

“B3.3.1 A financial liability (or part of it) is extinguished when the debtor either:

- (a) discharges the liability (or part of it) by paying the creditor, normally with cash, other financial assets, goods or services; or
- (b) is legally released from primary responsibility for the liability (or part of it) either by process of law or by the creditor. (If the debtor has given a guarantee this condition may still be met.)”

“B3.3.4 If a debtor pays a third party to assume an obligation and notifies its creditor that the third party has assumed its debt obligation, the debtor does not derecognise the debt obligation unless the condition in paragraph B3.3.1(b) is met. If the debtor pays a third party to assume an obligation and obtains a legal release from its creditor, the debtor has extinguished the debt. However, if the debtor agrees to make payments on the debt to the third party or direct to its original creditor, the debtor recognises a new debt obligation to the third party.”

The Committee notes from the above that under Ind AS 109, legal release from an obligation extinguishes the liability. It may also be noted that if, concurrently, an entity assumes another obligation to a third party or indeed to the original creditor, the new obligation also needs to be recognised. The Committee notes from the proposed Facts of the Case that the NCDs are novated by the Company to the SPV. As mentioned in paragraphs 5 and 6 above, the GoI, the parent of the SPV and the Company, has also given a letter of assurance to the SPV that it will provide necessary funds for payment of principal and interest on the NCDs novated to SPV to the extent of shortfall at the time of repayment. The Committee also notes that the querist has also mentioned in the facts of the case that after novation, the Company is legally released from the obligation towards the NCD holders.

From the above, the Committee is of the view that upon the novation of the NCDs (which is presumed to be from the date of Framework Agreement becoming legally effective, as mentioned in paragraph 11 above), the Company is legally released from its liability towards the NCD holders and therefore, the same should be derecognised by the Company. Similarly, when the funds of INR 22,064 crores are received by the Company from the SPV and the liabilities in the form of loans/ credit facilities from banks, are also settled, these should be derecognised.

Further, as a part of the Framework Agreement referred to in paragraph 7 above, pursuant to the Asset Transfer clause, the Company is required to transfer the non-core assets along with the debts transferred as discussed above.

The Committee also notes that although paragraph 3.3.3 of Ind AS 109 reproduced above, relating to derecognition of financial liability does not explicitly require the fulfilment of derecognition criteria for non-cash assets given as part of the consideration paid to be treated as part of the transfer, it is critical to determine whether the non-cash assets are given merely as collateral to the original creditor or as consideration for discharging the debtor from its liability towards the original creditor. Therefore, now the Committee proceeds to evaluate the

fulfilment of derecognition criteria under applicable Ind ASs for its non-core assets that comprise both non-financial assets (consisting of immovable properties) as well as financial assets (investments in equity shares of the identified subsidiaries).

In this context, the Committee notes that Ind AS 16 provides the following guidance with regard to disposal of property, plant and equipment:

“67 The carrying amount of an item of property, plant and equipment shall be derecognised:

(a) on disposal; or

(b) when no future economic benefits are expected from its use or disposal.”

“69 The disposal of an item of property, plant and equipment may occur in a variety of ways (eg by sale, by entering into a finance lease or by donation). The date of disposal of an item of property, plant and equipment is the date the recipient obtains control of that item in accordance with the requirements for determining when a performance obligation is satisfied in Ind AS 115. Ind AS 116 applies to disposal by a sale and leaseback.”

Further, Ind AS 40 provides the following guidance with regard to disposal of investment properties:

“66 An investment property shall be derecognised (eliminated from the balance sheet) on disposal or when the investment property is permanently withdrawn from use and no future economic benefits are expected from its disposal.

67 The disposal of an investment property may be achieved by sale or by entering into a finance lease. The date of disposal for investment property that is sold is the date the recipient obtains control of the investment property in accordance with the requirements for determining when a performance obligation is satisfied in Ind AS 115. Ind AS 116 applies to a disposal effected by entering into a finance lease and to a sale and leaseback.”

Ind AS 115 provides the following guidance with regard to transfer of control at a point in time:

“33 ...Control of an asset refers to the ability to direct the use of, and obtain substantially all of the remaining benefits from, the asset. Control includes the ability to prevent other entities from directing the use of, and obtaining the benefits from, an asset. ...”

“38 If a performance obligation is not satisfied over time in accordance with paragraphs 35– 37, an entity satisfies the performance obligation at a point in time. To determine the point in time at which a customer obtains control of a promised asset and the entity satisfies a performance obligation, the entity shall consider the requirements for control in paragraphs 31–34. In addition, an 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—if a customer is presently obliged to pay for an asset, then that may indicate that the customer has obtained the ability to direct the use of, and obtain substantially all of the remaining benefits from, the asset in exchange.

- (b) The customer has legal title to the asset—legal title may indicate which party to a contract has the ability to direct the use of, and obtain substantially all of the remaining benefits from, an asset or to restrict the access of other entities to those benefits. Therefore, the transfer of legal title of an asset may indicate that the customer has obtained control of the asset. If an entity retains legal title solely as protection against the customer’s failure to pay, those rights of the entity would not preclude the customer from obtaining control of an asset.
- (c) The entity has transferred physical possession of the asset—the customer’s physical possession of an asset may indicate that the customer has the ability to direct the use of, and obtain substantially all of the remaining benefits from, the asset or to restrict the access of other entities to those benefits. However, physical possession may not coincide with control of an asset. For example, in some repurchase agreements and in some consignment arrangements, a customer or consignee may have physical possession of an asset that the entity controls. Conversely, in some bill-and-hold arrangements, the entity may have physical possession of an asset that the customer controls. Paragraphs B64–B76, B77–B78 and B79–B82 provide guidance on accounting for repurchase agreements, consignment arrangements and bill-and-hold arrangements, respectively.
- (d) The customer has the significant risks and rewards of ownership of the asset—the transfer of the significant risks and rewards of ownership of an asset to the customer may indicate that the customer has obtained the ability to direct the use of, and obtain substantially all of the remaining benefits from, the asset. However, when evaluating the risks and rewards of ownership of a promised asset, an entity shall exclude any risks that give rise to a separate performance obligation in addition to the performance obligation to transfer the asset. For example, an entity may have transferred control of an asset to a customer but not yet satisfied an additional performance obligation to provide maintenance services related to the transferred asset.
- (e) The customer has accepted the asset—the customer’s acceptance of an asset may indicate that it has obtained the ability to direct the use of, and obtain substantially all of the remaining benefits from, the asset. To evaluate the effect of a contractual customer acceptance clause on when control of an asset is transferred, an entity shall consider the guidance in paragraphs B83–B86.”

The Committee notes from the documents supplied by the querist that on the Framework agreement becoming legally effective, the SPV shall have the rights on the rent and other income arising from the investment properties and the same shall be deposited in the escrow account created in favour of the SPV. Similarly, sale proceeds shall be deposited by the Company in the escrow account created in favour of the SPV. Although the legal title of the immovable properties has not been transferred to the SPV, the Company is obligated under the Framework Agreement to sell the properties and pass on the proceeds to the SPV. Therefore, the SPV has significant risks and rewards of ownership of the immovable properties after the Framework Agreement becomes legally effective. The de facto control is transferred on the Framework Agreement becoming effective and the creation of escrow account implies the proceeds/ income, if any, is held in trust for the SPV. Thus, upon the Framework Agreement becoming legally effective (which is also the effective date of transfer of assets, as mentioned in paragraph 11 above), the Company shall derecognise the immovable properties as a part of the non-cash consideration to the SPV towards the assumption by it of NCD liability and infusion of Rs. 22,064 crores into the Company.

The Committee also notes that the non-core assets also consist of investment in equity shares of identified subsidiaries of the Company. The Committee notes the following provisions of paragraph 10 of Ind AS 27, 'Separate Financial Statements' relating to accounting for its investments in subsidiaries:

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

- (a) at cost, or**
- (b) in accordance with Ind AS 109.**

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

In this context, the Committee notes from the annual report for the company for the financial year 2018-19 that the investments in subsidiaries are carried at cost, less impairment losses, if any. The Committee also notes that apart from the above requirements, Ind AS 27 does not specifically deal with the derecognition of investment in subsidiaries. In this context, the Committee also notes that Ind AS 109 provides the following scope exclusion in respect of interests in subsidiaries that are accounted for at cost in accordance with the requirements of Ind AS 27:

“2.1 This Standard shall be applied by all entities to all types of financial instruments except:

- (a) those interests in subsidiaries, associates and joint ventures that are accounted for in accordance with Ind AS 110 *Consolidated Financial Statements*, Ind AS 27 *Separate Financial Statements* or Ind AS 28 *Investments in Associates and Joint Ventures*. However, in some cases, Ind AS 110, Ind AS 27 or Ind AS 28 require or permit an entity to account for an interest in a subsidiary, associate or joint venture in accordance with some or all of the requirements of this Standard. Entities shall also apply this Standard to derivatives on an interest in a subsidiary, associate or joint venture unless the derivative meets the definition of an equity instrument of the entity in Ind AS 32 *Financial Instruments: Presentation*.**

...”

From the above, the Committee is of the view that although Ind AS 109 does not deal with the accounting in respect of investment in subsidiaries measured at cost under Ind AS 27, an analogy can be drawn from the derecognition requirements of Ind AS 109 in the absence of specific requirements for derecognition of the investments in subsidiaries measured at cost in any other Standard. In this context, the Committee notes that Ind AS 109 provides following guidance for derecognition of financial assets:

“3.2.3 An entity shall derecognise a financial asset when, and only when:

- (a) the contractual rights to the cash flows from the financial asset expire,**
or

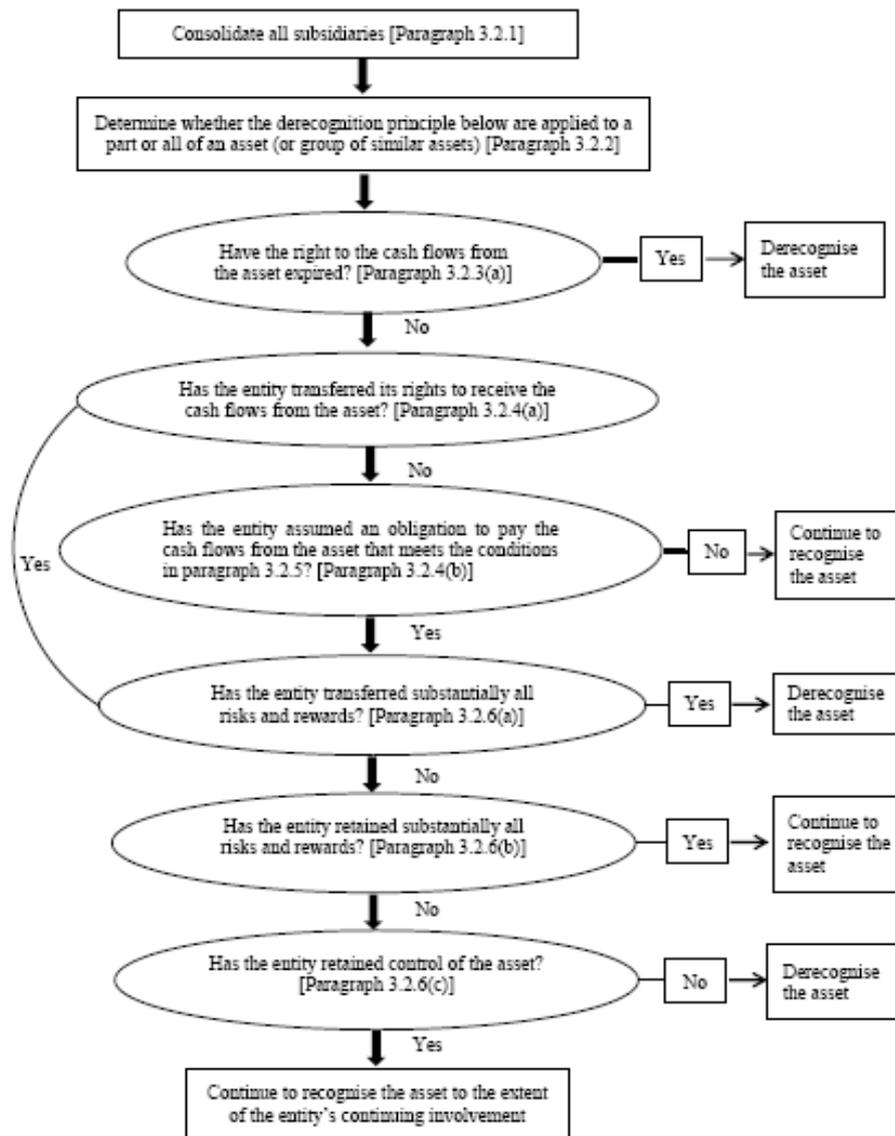
(b) it transfers the financial asset as set out in paragraphs 3.2.4 and 3.2.5 and the transfer qualifies for derecognition in accordance with paragraph 3.2.6.”

“3.2.12 On derecognition of a financial asset in its entirety, the difference between:

- (a) the carrying amount (measured at the date of derecognition) and
- (b) the consideration received (including any new asset obtained less any new liability assumed)

shall be recognised in profit or loss.”

“B3.2.1 The following flow chart illustrates the evaluation of whether and to what extent a financial asset is derecognised.



Arrangements under which an entity retains the contractual rights to receive the cash flows of a financial asset, but assumes a contractual obligation to pay the cash flows to one or more recipients (paragraph 3.2.4(b))

B3.2.2 The situation described in paragraph 3.2.4(b) (when an entity retains the contractual rights to receive the cash flows of the financial asset, but assumes a contractual obligation to pay the cash flows to one or more recipients) occurs, for example, if the entity is a trust, and issues to investors beneficial interests in the underlying financial assets that it owns and provides servicing of those financial assets. In that case, the financial assets qualify for derecognition if the conditions in paragraphs 3.2.5 and 3.2.6 are met.

B3.2.3 In applying paragraph 3.2.5, the entity could be, for example, the originator of the financial asset, or it could be a group that includes a subsidiary that has acquired the financial asset and passes on cash flows to unrelated third party investors.

Evaluation of the transfer of risks and rewards of ownership (paragraph 3.2.6)

B3.2.4 Examples of when an entity has transferred substantially all the risks and rewards of ownership are:

- (a) an unconditional sale of a financial asset;
- (b) a sale of a financial asset together with an option to repurchase the financial asset at its fair value at the time of repurchase; and
- (c) a sale of a financial asset together with a put or call option that is deeply out of the money (ie an option that is so far out of the money it is highly unlikely to go into the money before expiry).

B3.2.5 Examples of when an entity has retained substantially all the risks and rewards of ownership are:

- (a) a sale and repurchase transaction where the repurchase price is a fixed price or the sale price plus a lender's return;
- (b) a securities lending agreement;
- (c) a sale of a financial asset together with a total return swap that transfers the market risk exposure back to the entity;
- (d) a sale of a financial asset together with a deep in-the-money put or call option (ie an option that is so far in the money that it is highly unlikely to go out of the money before expiry); and
- (e) a sale of short-term receivables in which the entity guarantees to compensate the transferee for credit losses that are likely to occur.

B3.2.6 If an entity determines that as a result of the transfer, it has transferred substantially all the risks and rewards of ownership of the transferred asset, it does not recognise the transferred asset again in a future period, unless it reacquires the transferred asset in a new transaction.”

The Committee notes from the Facts of the Case that on the Framework Agreement becoming legally effective, the SPV shall have the rights on the identified subsidiaries. Although the legal title of the shares of the identified subsidiaries may not have been immediately transferred to the SPV, the Company is obligated under the Framework Agreement to transfer the identified subsidiaries to the SPV. Further, the Company is obligated to transfer the dividend, if any, received from the subsidiaries into the escrow account in favour of the SPV. Thus, once the Framework Agreement becomes legally effective, the SPV has significant risks and rewards of ownership of the subsidiaries. It can be said that the Company is holding the

investment in subsidiaries in trust on behalf of the SPV until they are legally transferred to the SPV. Therefore, upon the Framework Agreement being legally effective, the Company shall derecognise the investment in identified non-core subsidiaries as a part of the non-cash consideration to the SPV towards the assumption by it of NCD liability and infusion of Rs. 22,064 crores into the Company.

16. The Committee notes that the next question that arises is whether as per the requirements of paragraph 3.3.3 of Ind AS 109, on extinguishment/transfer of financial liability to another party by payment of consideration through transfer of any non-cash assets or liabilities assumed, the non-cash assets transferred are to be measured at their carrying amount or at fair value. In this context, the Committee notes that Ind AS 109 does not provide any specific guidance in this respect. Therefore, the Committee notes the requirements of other relevant Ind ASs, viz., Ind AS 16 and Ind AS 40 as follows:

Ind AS 16

“71 The gain or loss arising from the derecognition of an item of property, plant and equipment shall be determined as the difference between the net disposal proceeds, if any, and the carrying amount of the item.

72 The amount of consideration to be included in the gain or loss arising from the derecognition of an item of property, plant and equipment is determined in accordance with the requirements for determining the transaction price in paragraphs 47-72 of Ind AS 115. Subsequent changes to the estimated amount of the consideration included in the gain or loss shall be accounted for in accordance with the requirements for changes in the transaction price in Ind AS 115.”

Ind AS 40

“69 Gains or losses arising from the retirement or disposal of investment property shall be determined as the difference between the net disposal proceeds and the carrying amount of the asset and shall be recognised in profit or loss (unless Ind AS 116 requires otherwise on a sale and leaseback) in the period of the retirement or disposal.

70 The amount of consideration to be included in the gain or loss arising from the derecognition of an investment property is determined in accordance with the requirements for determining the transaction price in paragraphs 47-72 of Ind AS 115. Subsequent changes to the estimated amount of the consideration included in the gain or loss shall be accounted for in accordance with the requirements for changes in the transaction price in Ind AS 115.”

The Committee further notes that Ind AS 115 provides the following requirements for non-cash consideration:

“Non-cash consideration

66 To determine the transaction price for contracts in which a customer promises consideration in a form other than cash, an entity shall measure the non-cash consideration (or promise of non-cash consideration) at fair value.

67 If an entity cannot reasonably estimate the fair value of the non-cash consideration, the entity shall measure the consideration indirectly by reference to the stand-alone selling price of the goods or services promised to the customer (or class of customer) in exchange for the consideration.

- 68 The fair value of the non-cash consideration may vary because of the form of the consideration (for example, a change in the price of a share to which an entity is entitled to receive from a customer). If the fair value of the non-cash consideration promised by a customer varies for reasons other than only the form of the consideration (for example, the fair value could vary because of the entity's performance), an entity shall apply the requirements in paragraphs 56–58.
- 69 If a customer contributes goods or services (for example, materials, equipment or labour) to facilitate an entity's fulfilment of the contract, the entity shall assess whether it obtains control of those contributed goods or services. If so, the entity shall account for the contributed goods or services as non-cash consideration received from the customer."

Based on the above guidance, the Committee is of the view that the consideration given in the form of non-cash assets as per paragraph 3.3.3 of Ind AS 109 should be measured at their fair value at the time of the Framework Agreement becoming legally effective, which is also the effective date of transfer of assets.

The subsequent transactions (i.e., after derecognition/transfer) related to sale of immovable property are carried out by the Company on behalf of the SPV. The Company neither has any rights on the sale proceeds nor has guaranteed any minimum sale proceeds to the SPV. The sale proceeds are to be deposited in the escrow accounts. Therefore, these transactions shall not affect the statement of profit and loss or the equity of the Company.

17. With regard to the treatment of difference between the financial liabilities extinguished/transferred and the consideration paid in the form of non-cash assets, which is referred to as 'contribution' by the querist, the Committee notes that the Framework for the Preparation and Presentation of Financial Statements in accordance with Indian Accounting Standards² states that:

- "70 The elements of income and expenses are defined as follows:
- (a) Income is increases in economic benefits during the accounting period in the form of inflows or enhancements of assets or decreases of liabilities that result in increases in equity, other than those relating to contributions from equity participants.
- ... "

The Committee notes from the above that contributions from equity participants should not be considered as 'income' in the Statement of Profit and Loss.

In the extant case, the Committee notes from the Facts of the Case that the transfer of liabilities and assets are undertaken as a part of financial support to the Company by the GoI, monetizing of non-core assets of the Company and reducing the obligations/ liabilities with a view to achieve an operational / financial turnaround of the Company. The querist has specifically mentioned that "the SPV is acting on behalf of the GoI and as such the contributions can be considered to be made by the GoI itself, albeit through a Company owned 100% by the GoI itself. Hence, in substance, the financial assistance is in the nature of an equity contribution from the GoI".

² Framework for the Preparation and Presentation of Financial Statements in accordance with Indian Accounting Standards was replaced by Conceptual Framework for Financial Reporting under Indian Accounting Standards (Ind AS), which is applicable for Standard-setting activity with effect from April 1, 2020 and for Preparers of financial statements for accounting periods beginning on or after April 1, 2021.

The Committee notes that, in effect, as a result of the proposed financial restructuring, the SPV (which is also owned by the GoI) is taking over identified debt and identified non-core assets of the Company for the purpose of meeting the objective as set out in the Framework Agreement. The Committee also understands from the clause 2.5 of the Framework Agreement that the difference/deficit (if any) between the liabilities taken over by the SPV and the net proceeds of the assets transferred, shall be met by the GoI through capital grant. The financial restructuring pursuant to the Framework Agreement, therefore, in substance, results in a contribution from the equity participant – GoI as the obligation to repay the shortfall is transferred to an SPV owned by the GoI.

From the above and considering that both the Company and the SPV respectively, are 100% owned by the GoI, the Committee is of the following view:

- (i) The derecognition of financial liabilities of the Company, viz., NCDs and other liability of Rs. 22,064 crores, in substance, is a transaction at the behest of the equity shareholders (GoI) as a part of financial restructuring plan. Therefore, considering the fact that the GoI in the extant case is acting in its capacity as equity shareholder, the difference between the financial liabilities extinguished/transferred and the consideration paid in the form of non-cash assets shall be accounted for as an equity contribution by the equity participant.
- (ii) At the date of Framework Agreement becoming legally effective, the difference between the carrying amounts and the fair values of the immovable properties and investment in identified subsidiaries, i.e., gain or loss on derecognition of the above-mentioned assets shall be recognised in Statement of Profit and Loss. It would not be appropriate to present this difference as equity contribution by the equity participant.

18. Further, with regard to the issue raised by the querist in paragraph 10 (ii) above relating to government grant, the Committee notes the following paragraphs of Indian Accounting Standard (Ind AS) 20, 'Accounting for Government Grants and Disclosure of Government Assistance':

“Government refers to government, government agencies and similar bodies whether local, national or international.

Government assistance is action by government designed to provide an economic benefit specific to an entity or range of entities qualifying under certain criteria. Government assistance for the purpose of this Standard does not include benefits provided only indirectly through action affecting general trading conditions, such as the provision of infrastructure in development areas or the imposition of trading constraints on competitors.

Government grants are 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. They exclude those forms of government assistance which cannot reasonably have a value placed upon them and transactions with government which cannot be distinguished from the normal trading transactions of the entity.

“Scope

- 2 This Standard does not deal with:

- (a) the special problems arising in accounting for government grants in financial statements reflecting the effects of changing prices or in supplementary information of a similar nature.
- (b) government assistance that is provided for an entity in the form of benefits that are available in determining taxable profit or tax loss, or are determined or limited on the basis of income tax liability. Examples of such benefits are income tax holidays, investment tax credits, accelerated depreciation.
- (c) government participation in the ownership of the entity.
- (d) government grants covered by Ind AS 41, *Agriculture*.”

Ind AS 20, unlike AS 12, ‘Accounting for Government Grants’, does not recognise government grants of the nature of promoters’ contribution. Ind AS 20 is based on the principle that all government grants would normally have certain obligations attached to them and it, accordingly, requires all grants to be recognised as income over the periods which bear the cost of meeting the obligation or it also provides alternative approach of treating such grant from the cost of the asset.

The Committee is of the view that if government provides support to an entity and is also an equity shareholder/owner of equity instruments in that entity, then an assessment needs to be carried out as to whether the government is acting in its capacity as shareholder/owner or as government. If there is no requirement attached to a contribution from the government to comply with certain conditions relating to the operating activities of the entity, then that contribution is most likely not a government grant. Also, generally, grant is not issued in isolation, it is offered to other companies also in the industry. Based on the above analysis, the Committee is of the view that the Company’s observation that “in substance, the financial assistance is in nature of an equity contribution from the GoI” is correct and hence, financial assistance from the Government through SPV in the extant case shall not be treated as a government grant.

D. Opinion

19. On the basis of the above and subject to presumptions and premises discussed in paragraph 11 above, the Committee is of the following opinion on the issues raised by the querist in paragraph 10 above:

- (i) Referring to the discussion in paragraphs 13 to 17 above, the accounting proposed by the querist is not in line with the requirements of Indian Accounting Standards.
- (ii) Referring to discussion in paragraph 18 above, financial assistance by the Government through SPV should not be treated as a government grant. Hence the accounting treatment for government grants shall not be applied.
- (iii) The Company shall follow the following accounting treatment upon the Framework Agreement becoming legally effective:
 - (a) The Company shall derecognise the NCDs and other financial liability due to SPV and derecognise the immovable properties and investments in identified subsidiaries;
 - (b) The difference between NCDs derecognised and the other liability of Rs. 22,064 crores in respect of funds received from the SPV, on one hand, and the fair value of the non-core assets (immovable properties and investments in identified subsidiaries), on the other hand, represents shareholder’s contribution and hence shall be recognised directly in equity under “Other Equity”.

- (c) The difference between the fair value and the carrying amount of the non-core assets (immovable properties and investments in identified subsidiaries) should be recognised in the Statement of Profit and Loss.
-