

Query No. 22

Subject: Derecognition of loan portfolio as a result of securitization.¹

A. Facts of the Case

1. A Company (hereinafter referred to as ‘the Company’) is a subsidiary of a Housing Finance Company, registered with the National Housing Bank (NHB) under section 29A of the National Housing Bank Act, 1987 and is primarily engaged in lending of housing loans.

2. Hitherto till 31st March 2018, the Company was preparing and presenting its financial statements as per the Companies (Accounting Standards) Rules, 2006 and other applicable regulatory guidelines. However, due to an amendment in section 133 of the Companies Act, 2013, it is now, with effect from the accounting year commencing on 1st April 2018, preparing and presenting its financial statements as per the Companies (Indian Accounting Standards) Rules, 2015 (Ind ASs).

3. Vide assignment agreement dated 29th March 2019, the Company assigned a part of its loan receivables portfolio, already classified as non-performing asset, amounting to Rs. 3038.13 lakhs for a value of Rs. 2278.60 lakhs to ABC Trust (special purpose vehicle) which has been declared a trust in accordance with Indian Trusts Act, 1882 by XYZ ARC (Asset Reconstruction Company) who is its trustee also. The Trust thereafter issued security receipts (SRs) in the ratio of 85:15, i.e., of Rs. 1936.81 lakhs to the Company and Rs. 341.79 lakhs to XYZ ARC. The transaction was carried out in compliance with the Reserve Bank of India (RBI) norms for securitization.

4. Accordingly, when presenting the financial statements as at 31st March 2019, the Company de-recognized the loan receivables portfolio by Rs. 3038.13 lakhs and recognized the SRs issued by the Trust at Rs. 1936.81 lakhs. As on the date of assignment, the Company, with respect to aforesaid portfolio, had a provision of expected credit loss of Rs. 856.31 lakhs. The assignment of loan portfolio consequently resulted into a gain of Rs. 96.78 lakhs that was presented under appropriate line item in the audited financial statements as at and for the year ended 31st March 2019.

5. In the aforesaid financial statements, the Company explained the aforesaid transaction in Note no. 40(2) in notes to the financial statements as under:

“(2) During the year, the Company has entered into a transaction with the ABC Trust (special purpose vehicle) wherein it has sold GNPA of INR 3038.13 lakhs for a value of INR 2278.60 lakhs. The transaction has been carried out in compliance with the applicable RBI norms for securitization and the Trust has issued security receipts (SR) in the ratio of 85:15 i.e. of INR 1936.81 lakhs to the company and INR 341.79 lakhs to XYZ ARC. The transaction is concluded within the RBI purview and the Company has obtained true sale opinion for concluding the transaction.

Accordingly, the Company has derecognized the NPA loan receivables and has recognized security receipts as investments in the books of accounts. The Company shall recognize profit/loss on the Security Receipts based on the evaluation by independent rating agency as stipulated under RBI Regulation.

Under Ind AS, the security receipts issued by the trust would fulfil the criteria for a financial asset and has been recognized in its books.”

¹ Opinion finalised by the Committee on 10.11.2020.

The Company also obtained a legal opinion dated 1st April 2019 from its legal advisors who opined as under:

“The assignment of the receivables by the Assignor to the Assignee in the manner contemplated in the transaction documents will constitute an absolute assignment and transfer (ie a sale or true sale) and will convey to the Assignee a legally enforceable right in the debts / actionable claims assigned to it.”

6. However, the statutory auditors of the Company in their ‘Independent Auditors Report to the Members of the Company’ dated 20th May 2019 gave a qualified opinion with respect to aforesaid transaction as under:

“We draw attention to Note 40(2) of the financial statements in relation to transaction with a trust namely ABC Trust (special purpose vehicle) wherein Gross NPA of Rs. 3038.13 lakhs were sold for a value of Rs. 2278.60 lakhs & Trust has issued security receipts (SR) in the ratio of 85:15. As informed by Company, based on the legal opinion obtained, it was a true sale. Considering that, Company has derecognized NPA loan receivables and has recognized security receipts as investments in the books of account. As per Ind AS 109, derecognition of financial assets shall take place only if substantial risk and reward has been transferred. However, in the referred transaction of security receipts, the Company may remain exposed to substantial risk of return.

Had these NPA loan receivables not been derecognized, classification of loans into investments would not have changed and profit for the year would have decreased by Rs. 96.78 lakhs.”

7. The statutory auditors continued to maintain their viewpoint. In their modified audit report for the year ended 31st March 2020 they mentioned as under:

“We draw attention to Note 39(2) (read with the modified report dated 20th May 2019 for the year ended March 31, 2019) of the Ind AS financial statements in relation to transaction with a trust namely ABC Trust (special purpose vehicle) wherein during F.Y. 2018–19, Gross NPA of Rs. 3038.13 lakhs were sold for a value of Rs. 2278.60 lakhs and Trust has issued security receipts (SR) in the ratio of 85:15. As informed by Company, based on the legal opinion obtained, it was a true sale. Considering that, Company has derecognized NPA loan receivables and has recognized security receipts as investments in the books of account. As per Ind AS 109, derecognition of financial assets shall take place only if substantial risk and reward has been transferred. However, in the referred transaction of security receipts, the Company may remain exposed to substantial risk of return.

Had these NPA loan receivables not been derecognized, classification of loans into investments would not have changed and profit for the year ended 31st March 2019 would have decreased by Rs. 96.78 lakhs.

Had these NPA loan receivables not been derecognized as on 31st March 2020, classification of loans into investments would not have changed and profit for the year ended 31st March 2020 would have decreased by Rs. 128.02 lakhs.”

8. The querist has stated that it is apparent from the aforesaid that the statutory auditors in their basis for qualified opinion relied only on the risk & reward test as enumerated in section 3.2 (Derecognition of Financial Assets) read with applicable implementation guidance of Ind AS 109. The said section / implementation guidance lays down 2 tests:

- Risk & reward test;

- Control test.

First risk & reward test has to be applied. If that fails, then control test has to be applied. In the present case, according to the querist, not only control test but risk & reward test also stands satisfied, as explained in Annexure A.

9. Various arguments as to why treatment is in accordance with the applicable Accounting Standard has also been put forth by the Company, which are contained in Annexure A.

10. The Company in its support has provided the following documents:

- Declaration of Trust deed dated 28th March 2019;
- Assignment Agreement dated 29th March 2019 between the Company and ARC (SPV);
- Security Receipts (SRs) Offer Document issued by the Trust dated 29th March 2019;
- Bid dated 29th March 2019 for purchase of NPAs of Company;
- Legal opinion dated 1st April 2019 on 'Securitization of Loan Receivables' by M/s xyz Advocates;
- Audited annual accounts as at and for the year ended 31st March 2019;
- Audited annual accounts as at and for the year ended 31st March 2020;
- RBI Guidelines on sale of financial assets to Securitization Company (SC)/RC-DBOD No.BP.BC. 96/ 21.04.048/ 2002-03 dated 23 April 2003;
- RBI communication no. RBI/2011 – 12/540; DBOD. No. BP.BC – 103/21.04.177/2011 – 12 dated 7th May 2012;
- RBI Communication-RBI 2015-1694 DNBR.(PD).CC.No. 03SCRC26.03.0012015-16;
- Service Provider Agreement dated 8th May 2019.

B. Query

11. In the light of the above, the opinion of the Expert Advisory Committee has been sought as to whether the Company has correctly derecognized the loan portfolio and recognized the SRs as investments as per the applicable provisions of Ind AS particularly Ind AS 109, 'Financial Instruments'.

C. Points considered by the Committee

12. The Committee notes that the basic issue raised in the query relates to whether derecognition of the loan receivables in the separate financial statements of the Company as a result of assignment of such receivables to a Special Purpose Vehicle against consideration in form of cash/ security receipts is appropriate or not. 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, classification, recognition, measurement (initial and subsequent) and presentation of loan receivables, impairment of loan receivables including accounting for provision of expected credit loss in the financial statements of the Trust or ARC, accounting for fees collected by the Company as a service agent to the SPV, accounting for cash/SRs received by the Company on assignment of loan receivables, tax treatment of the transaction, compliance with the securitization guidelines and other Acts/Guidelines/Circulars, issued by the Reserve Bank of India/ National Housing Bank etc. Further, the Committee has not examined whether the Trust (SPV) needs to be included or consolidated in the financial statements of the Company as per the requirements of the relevant Ind ASs, such as, Ind AS 110, 'Consolidated Financial Statements'. The Committee also wishes to point out that the opinion expressed hereinafter is in the context of Indian Accounting Standards, notified under the Companies (Indian Accounting Standards) Rules, 2015 as amended from time to time. Further, the opinion expressed hereinafter is purely from accounting perspective and not from the

perspective of legal interpretation of various legal enactments, such as, Indian Trusts Act, securitization guidelines and other Acts/Guidelines/Circulars, issued by Reserve Bank of India/National Housing Bank, etc.

13. The Committee notes from the various documents provided by the querist that assignment deed was entered into pursuant to bid acceptance document dated 29th March 2019 and in terms of the bid document, the Company was paid 15% of the assigned value by way of cash by the SPV and balance 85% in terms of the Security Receipts (SRs). The ABC Trust through its Trustee (XYZ ARC) issued an Offer Document dated 29th March 2019 for issuance of the security receipts (SRs) to the extent of the purchase or assigned value of the loan receivable portfolio. The ARC contributed 15% of the assignment value by cash and was issued security receipts against its contribution with balance 85% to the Company as aforesaid. The transaction of assignment was consummated on 29th March 2019 on assignment of loan portfolio being completed and consideration having been received in terms of cash/ SRs of the SPV trust.

14. In the context of the issue raised, the Committee notes the following requirements of Indian Accounting Standard (Ind AS) 109:

“3.2 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.

(See paragraph 3.1.2 for regular way sales of financial assets.)

3.2.4 An entity transfers a financial asset if, and only if, it either:

- (a) transfers the contractual rights to receive the cash flows of the financial asset, or
- (b) 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 in an arrangement that meets the conditions in paragraph 3.2.5.

...

3.2.6 When an entity transfers a financial asset (see paragraph 3.2.4), it shall evaluate the extent to which it retains the risks and rewards of ownership of the financial asset. In this case:

- (a) if the entity transfers substantially all the risks and rewards of ownership of the financial asset, the entity shall derecognise the financial asset and recognise separately as assets or liabilities any rights and obligations created or retained in the transfer.
- (b) if the entity retains substantially all the risks and rewards of ownership of the financial asset, the entity shall continue to recognise the financial asset.

- (c) **if the entity neither transfers nor retains substantially all the risks and rewards of ownership of the financial asset, the entity shall determine whether it has retained control of the financial asset. In this case:**
 - (i) **if the entity has not retained control, it shall derecognise the financial asset and recognise separately as assets or liabilities any rights and obligations created or retained in the transfer.**
 - (ii) **if the entity has retained control, it shall continue to recognise the financial asset to the extent of its continuing involvement in the financial asset (see paragraph 3.2.16).**

3.2.7 The transfer of risks and rewards (see paragraph 3.2.6) is evaluated by comparing the entity's exposure, before and after the transfer, with the variability in the amounts and timing of the net cash flows of the transferred asset. An entity has retained substantially all the risks and rewards of ownership of a financial asset if its exposure to the variability in the present value of the future net cash flows from the financial asset does not change significantly as a result of the transfer (eg because the entity has sold a financial asset subject to an agreement to buy it back at a fixed price or the sale price plus a lender's return). An entity has transferred substantially all the risks and rewards of ownership of a financial asset if its exposure to such variability is no longer significant in relation to the total variability in the present value of the future net cash flows associated with the financial asset (eg because the entity has sold a financial asset subject only to an option to buy it back at its *fair value* at the time of repurchase or has transferred a fully proportionate share of the cash flows from a larger financial asset in an arrangement, such as a loan sub-participation, that meets the conditions in paragraph 3.2.5).

3.2.8 Often it will be obvious whether the entity has transferred or retained substantially all risks and rewards of ownership and there will be no need to perform any computations. In other cases, it will be necessary to compute and compare the entity's exposure to the variability in the present value of the future net cash flows before and after the transfer. The computation and comparison are made using as the discount rate an appropriate current market interest rate. All reasonably possible variability in net cash flows is considered, with greater weight being given to those outcomes that are more likely to occur.

3.2.9 Whether the entity has retained control (see paragraph 3.2.6(c)) of the transferred asset depends on the transferee's ability to sell the asset. If the transferee has the practical ability to sell the asset in its entirety to an unrelated third party and is able to exercise that ability unilaterally and without needing to impose additional restrictions on the transfer, the entity has not retained control. In all other cases, the entity has retained control.

Transfers that qualify for derecognition

3.2.10 If an entity transfers a financial asset in a transfer that qualifies for derecognition in its entirety and retains the right to service the financial asset for a fee, it shall recognise either a servicing asset or a servicing liability for that servicing contract. If the fee to be received is not expected to compensate the entity adequately for performing the servicing, a servicing liability for the servicing obligation shall be recognised at its fair value. If the fee to be received is expected to be more than adequate compensation for the servicing,

a servicing asset shall be recognised for the servicing right at an amount determined on the basis of an allocation of the carrying amount of the larger financial asset in accordance with paragraph 3.2.13.

3.2.11 If, as a result of a transfer, a financial asset is derecognised in its entirety but the transfer results in the entity obtaining a new financial asset or assuming a new financial liability, or a servicing liability, the entity shall recognise the new financial asset, financial liability or servicing liability at fair value.

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.”

“Transfer that do not qualify for derecognition

3.2.15 If a transfer does not result in derecognition because the entity has retained substantially all the risks and rewards of ownership of the transferred asset, the entity shall continue to recognise the transferred asset in its entirety and shall recognise a financial liability for the consideration received. In subsequent periods, the entity shall recognise any income on the transferred asset and any expense incurred on the financial liability.”

“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.”

15. The Committee notes from the above that a financial asset is derecognized when and only when either the contractual rights to the asset’s cash flows expire, or the asset is transferred, and the transfer qualifies for derecognition. This decision of whether a transferred asset qualifies for derecognition is made by applying a combination of ‘risks and rewards’ and ‘control’ tests. Derecognition cannot be achieved by only a legal transfer. The transfer must happen in substance which is evaluated by using ‘risks and rewards’ and ‘control’ model. The question for the consideration of the Committee is whether in the facts of the case, the assignment of loan receivables portfolio by the Company in favour of SPV (Trust) where the Company has 85% share in all outstanding Security Receipts of the SPV qualifies for derecognition of financial asset i.e. whether it satisfies one of the conditions laid down.

16. In this context, the Committee reviewed the documents provided by the Company and notes the following relevant facts/clauses from each of the documents:

A. Bid Acceptance document dated 29th March 2019

- I. Offer for the pool of NPAs is on Cash cum Security Receipts basis.
- II. Assignment value was determined at 75% of Principal Outstanding Amount.
- III. The cash portion of the offer @ 15% of the offer amount will be paid by SPV.
- IV. Company will subscribe to the balance 85% of the Offer amount by way of Security Receipts (SR), which shall be issued by the Trust.
- V. The Terms of the SR would include:
 - a. 15% of the subscription amount would be paid by ARC.
 - b. The tenure of the SRs will be 5 years, extendable (as per the prevailing RBI guidelines).
 - c. Management fee, which shall be calculated as 2% per annum, will be paid to ARC.
 - d. SRs will have paripassu redemption among the beneficiaries in proportion to their holding.
 - e. Incentive on recovery amount, net of all expenses & management fee will be paid to ARC ranging from 3.5% in year 1 to 1% in year 5.
 - f. Collection Costs: 6% plus applicable taxes. In terms of Offer document, the Company has been designated as the service agent. Further, the collection fee will be paid to Company in terms of service agreement dated 8th May 2019.
 - g. Excess recovery after redemption of security receipts i.e. upside, if any, will be shared by SR holders and ARC on 85:15 basis.

B. Offer Document dated 29th March 2019

The Prospective Investors will not have any recourse against the Sellers and/or the Trustee in respect of the transaction envisaged herein and the Transaction Documents, save and except to the extent of the Trust Fund, (which shall be distributed by the Trustee amongst the Security Receipt Holders in accordance with the terms contained herein and in the Trust Deed), on account of any reason whatsoever, including but not limited to:

(i) ...

(ii) any default or non-payment of any amount constituting the Assets by the Borrowers or any third party;

...

(v) any shortfall in the Assets, whether arising out of inadequate recovery or realization of the Assets or otherwise;

4.1 Objects of Offer

The primary objective of the Trust and the transaction contemplated under this Offer Document is to utilise the Contributions to acquire the Assets, described in Section 5.1 (*Description of the Financial Assets Proposed to be Acquired*)...

4.2.1 The Trust will issue to the Prospective Investors whose applications are accepted, the Security Receipts, which shall be called...

4.2.3 Each Security Receipts represents undivided right, title and interest in the Trust Fund, including the Initial Trust Fund, the contributions received by the Trustee, the Assets proposed to be acquired by the Trustee and will be issued pursuant to the terms of the Trust Deed and this Offer Document.

4.4 Probable Yield

Subject to provisions of Section 6.4 (*Distribution of amounts received by Trustee*), no yield is envisaged to be paid on the Security Receipts.

It should be noted that there are no returns guaranteed on the Security Receipts. The Trustee shall not be liable for any shortfall on any of the Security Receipts. It is therefore clarified that there shall be no obligation on the Trustee to make any distributions/payments on the Security Receipts, unless and until, monies are available for distribution by the Trustee.

4.7 Without Recourse

... Consequently, the Security Receipt Holders must rely solely on the amounts recovered from the Assets for any returns/distributions on the Security Receipts. ... If the Trust Fund, including all amounts received from the Assets, is insufficient to make distributions on the Security Receipts, no other assets of the Trustee or XYZ ARC will be available for payment of deficiency and following the realization/liquidation of all the Assets and termination of the Trust, the Trustee will have no further obligation in respect of the Security Receipts. ...

4.14 Meetings of Security Receipt Holders

The Trustee may, at its discretion, or shall, on a requisition of one or more of the Security Receipt Holders holding not less than 75% of the face value of all the then outstanding Security Receipts, convene a meeting of the Security Receipt Holders. *Provided that* the Trustee shall hold such meeting at a date not later than 45 (forty-five) days after it receives the requisition for convening such meeting. *Provided further*, the Security Receipts Holders can exercise the right to convene the meeting of the Security Receipt Holders in case of non-realisation of financial assets and subject to the provisions contained in the SARFAESI Act and the Guidelines issued by the Statutory Authority in this regard.

The Trustee shall give each Security Receipt Holder at least 15 (fifteen) days' notice in advance for any meeting of the Security Receipt Holders, specifying the purpose of the meeting in the notice.

Any decision requiring the consent/approval of the Security Receipt Holders shall be deemed to have been taken if the Security Receipt Holders holding not less than 75% of the face value of all the then outstanding Security Receipts, present and voting at such general meeting, vote in favour of such decision. *Provided that* any such decision requiring the consent and approval of the Security Receipt Holders may be obtained by a letter or letters, signed by the Security Receipt Holders holding not less than 75% of the face value of all the then outstanding Security Receipts without convening a meeting of the Security Receipt Holders as if such letter or letters constitute a resolution passed or decision taken at a meeting duly convened and held as aforesaid and shall have effect accordingly.

4.25 Revocation of Contribution

4.25.1 The Security Receipt Holders shall be entitled to revoke the Contributions made by them, at any time during the term of the Trust Deed, in accordance with the terms and conditions contained therein, for any reason, including but not limited to circumstances resulting from any adverse tax consequences (for either the Trust of the Security Receipt Holders) or any direction of any Statutory Authority, provided that no such revocation shall take effect unless the consent of the Security Receipt

Holders holding Security Receipts representing not less than 75% of the total value of the then outstanding Security Receipts issued pursuant to the Trust Deed has been obtained, in this behalf, provided that a notice not less than 60 days of the intention to revoke the contribution is given to the Trustee.

- 4.25.2 In the event that the Trustee, at any time faces any adverse tax consequences or upon any direction of any Statutory Authority, the Trustee shall have the right to call upon the Security Receipt Holders to revoke their Contributions as per applicable laws.
- 4.25.3 In the event that the Contributions are revoked in terms of the Trust Deed and this Offer Document, the Trust Fund shall automatically stand transferred as aforesaid, and shall automatically and without any further act, deed or writing, operate as an assignment vesting the Trust Fund jointly in favour of each of the Security Receipt Holders (in proportion to their Contributions) or to any Person designated by the Security Receipt Holders in this behalf provided that the Trustee has received payment of all Amounts Due or accrued to the trustee in full, in accordance with the terms of the Trust Deed. Upon such transfer all the provisions of the relevant Financing Documents and the Assignment Agreement shall apply *mutatis mutandis* to the Security Receipt Holders or their designee, and the Security Receipt Holders or their designee shall be entitled to all rights and remedies of the Trustee and shall be obliged to perform all its duties and obligations under the relevant Financing Documents and the Assignment Agreement, as if the Security Receipt Holders or their designee were party to the Financing Documents and the Assignment Agreement as of the date thereof,
- 4.25.4 The Security Receipt Holders and the Trustee hereby agree and undertake to execute further documents, deeds and writings as may be necessary to implement the aforesaid assignment and the other transactions set forth in the relevant Financing Documents and the Assignment Agreement, and may mutually negotiate in good faith with the relevant Borrower and agree upon the specific terms and conditions of implementation of the transaction contemplated thereby,

...

- 4.25.6 All costs, charges and expenses incurred or arising out of or consequent to the revocation of the Contributions and transfer of the Trust Fund unto the Security Receipt Holders, as mentioned above, shall be borne in by the Security Receipt Holders in proportion to their respective Contributions,

4.26 Tax Indemnity

Without prejudice to its right to require the Security Receipt Holders to revoke their Contributions in the manner specified in the Trust Deed, in the event of any adverse tax consequences on the Trust, the Trustee shall be entitled to require the Security Receipt Holders to bear such consequences in the ratio that the total face value of their respective Security Receipts bear to the total face value of the then outstanding Security Receipts, unless otherwise mutually agreed upon between the Trustee and the Security Receipt Holders.

5.1 Description of the Financial Assets

...

The Assets are currently owned by the Sellers and are proposed to be assigned to the Trustee. The Assets are SMA-2 or non-performing assets in the books of the Sellers, ...

5.4 Nature and Value of Underlying Security Interest, Expected Cash Flows, Quantum and Timing, Credit Enhancement Measures

- As given in the attached Annexure.

5.4.1 Underlying Security Interest: Nature and Value of Underlying Security Interest, Expected Cash Flows, Quantum and Timing, Credit Enhancement Measures; Underlying Security Interest

Prospective Investors should note that all the Security Interests mentioned in the table above do not secure the repayment of each of the Assets and that the Security Interests have only been clubbed for convenience. The underlying Security Interests have not been separately valued.

5.4.2 Expected Cash Flows, Quantum and Timing

The expected cash flows and their quantum and timing will depend on the resolution strategy formulated for the Assets during the Strategy Period.

5.4.3 Credit Enhancement Measures

Credit enhancement strategy, if any, shall be formulated during the strategy period.

6.4 Distribution of Amounts Received by the Trustee

6.4.1 Subject to Section 4.1 (*Objects of Offer*), on the relevant Payment Date, distribution of realisation from Financial Assets shall be on pari-passu basis, proportionate to the investment made by SR holders, subject to meeting specified expenses/liabilities in priority....

- (a) ...statutory liabilities and regulatory dues...
- (b) ...any reimbursable costs and expenses chargeable to Trust Fund (including for servicing of any debt incurred by the Trust)...
- (c) ...collection cost @ 6% on the collections made, to the relevant collection agent...
- (d) ...Management fee which shall be calculated as 2% per annum. The Management Fee shall accrue on a quarterly basis but will be payable only on the recovery on realisation of assets. For this purpose, the Management fee shall be calculated and as percentage of the quarterly closing Net Asset Value (NAV) at the lower end of such NAV specified by the Credit Rating Agency (CRA) provided that the same is not more than the acquisition value of underlying Financial Asset...
- (e) ...Incentive on net recovery amount will be given to ARC for early redemption of SR...
- (f) ...
- (g) ...payment of the amounts to be distributed amongst the Security Receipt Holders, listed in the Register of Security Receipt Holders, as on the relevant

Record Date corresponding to such Payment Date, in accordance with the terms and conditions of their respective Security Receipts. The amounts shall be paid to Security Receipt Holders on pro-rata basis to the extent of face value of Security Receipts held on the Payment Date.

(h) Excess recovery, if any, after the redemption of all the Security Receipts shall be shared by the ARC and the Initial Seller (in its capacity as Security Receipt Holder) on 15:85 basis.

...

6.5.3 Breakage Costs

Upon any revocation of the Trust...or upon any termination of the Trust by the Security Receipt Holders...breakage costs of an amount mutually agreed upon, as determined for the purpose of the most recent declaration of the Net Asset Value shall be paid to the Trustee.

6.6.1 Powers of the Trustee

The Trustee is vested with the general superintendence, direction and management of the affairs of the Trust. The following is an indicative list of the powers so exercisable by the Trustee, under the Trust Deed subject to prior consent of the Security Receipt Holders;

(i) ...

(ii) to collect all monies due to the Trust...

(iii) to distribute to the Security Receipt Holders, the Trust Fund, in accordance with the payment mechanism set out in ...this Offer document...

...

(xiii) to vary, add or otherwise alter all or any of the features of the scheme contemplated under this Offer Document and the Trust Deed with the prior written consent of Security Holders holding at least 90% in value of the then outstanding Security Receipts issued pursuant to the Assignment Agreement,

Any such Variation, addition or alteration shall be binding on all the Security Receipt Holders and any Person or Persons claiming through or under them as if each Security Receipt Holder or such Person expressly had agreed that such features and terms shall be so binding;

6.12 Role of Seller Post Acquisition of Assets

Subsequent to the acquisition of the Assets from the Sellers, the Sellers shall not retain any of the risk or rewards associated with the Assets. XYZ ARC, to manage the recoveries and accounting for the Assets or to give effect to the SARFAESI Act, may, if deemed expedient, retain the Sellers as agents for collection of the monies in relation to such Assets and determine their fees, including any incentive-based fee.

7.1 Statement of risk factors

7.1.2 Scheme Specific Risk Factors

Prospective Investors should also consider the following scheme-specific risk factors:

...

(e) Tax Issues

The Prospective Investors should note that the Trust has been established through revocable contributions and therefore, XYZ ARC has been advised that the income of the Trust would not be subject to tax. Section 61 read with Section 63 of the Income Tax Act, 1961, provides that any income arising from a revocable transfer of assets would be taxed in the hands of such transferor. In the present case, all the income of the Trust may be said to arise from the contributions of the Security Receipt Holders to the Trust and therefore all the income of the Trust would be distributed to the Security Receipt Holders and taxed in their hands, at the rate applicable to each such individual.

C. Assignment Deed dated 29th March 2019

2 ASSIGNMENT OF LOANS

2.1 Assignment

2.1.1 The Parties hereto acknowledge that the provisions of the SARFAESI Act including but not limited to Section 5(3) of the SARFAESI Act will be applicable and the conditions precedent Set forth in Clause 3 of this Agreement (*Conditions Precedent*) have been fulfilled or waived by the Assignee, as the case may be.

2.1.2 The Parties further acknowledge that, in consideration of the Assignee; paying the Purchase Consideration to the Assignor, upon the terms and conditions set forth herein and in the relevant Transaction Documents, the Assignor is the true, legal and beneficial owner of the Loans, in the ordinary course of its business and further hereby unconditionally and irrevocably sells, assigns, transfers and releases to and unto the Assignee all the Loans, pursuant to Section 5(1)(b) of the SARFAESI Act TO HOLD the same absolutely IN TRUST for the benefit of the Security Receipts Holders issued by the Assignee pursuant to the Trust Deed TO THE END AND INTENT THAT the Assignee shall hereafter be deemed to be the full and absolute legal owner, and the only person legally entitled to the Loans or any part thereof, on an “as is where is basis”, and to recover and receive all Amounts Due, including the right to file a suit or institute such other recovery proceedings, to continue with the recovery suits filed by the Assignor and take such other action as may be required for the purpose of recovery of the Loans, in its own name and right and as an assignee, and not as a representative or agent of the Assignor and to exercise all other rights of the Assignor in relation thereto.

2.1.5 The entire Purchase Consideration shall be paid by the Assignee to the Assignor by way of electronic funds transfer or remittance of funds or any other means by crediting the account number xxx of xx (bank), of the Assignor.

D. Declaration of Trust dated 28th March 2019

“**Trust Fund** means the Initial Trust Fund, the Contributions, the Loans and the Amounts Due, other Financial Assets relating to the Borrower(s), acquired by the Trust under the Assignment Agreements, the Trust Account and all sub-accounts of the same, all Permitted Investments of the Trust, all income and realisations made for and on behalf of the Trust and any other assets or property of the Trust.

2.1 Declaration of Trust

(a) The Declarant hereby declares, agrees, assures and confirms that the Declarant shall hereinafter HAVE AND HOLD a sum of Rs. 1000/- (Rupees One Thousand Only) (hereinafter referred to as the “**Initial Trust Fund**”)...

(b) The Trustee hereby further declares and confirms that the Trust Fund shall be held and possessed by the Trustee, in trust for the Security Receipt Holders upon acceptance of the Contributions from the Security Receipt Holder and in whose favour Security Receipts shall be issued by the Trustee...”

Trust Account

The Trustee shall forthwith deposit all amounts received by it, forming part of the Trust Fund in a bank account opened with a bank ..., which account, along with any sub-accounts thereunder, shall be held by the Trustee for the benefit of the Security Receipt Holders and shall form part of the Trust Fund. The Contributions deposited in this Trust Account shall be utilized for the payment, by the Trustee, of the Purchase Consideration under the Assignment Agreement...

2.7 Date of Termination of the Trust

2.7.1 The Trust will stand terminated on such date as the Trustee may determine in accordance with the SARFAESI Act, having regard to the maximisation of returns on the Security Receipts issued pursuant to this Deed, which shall, in no event, be later than the period specified under the SARFAESI Act in this regard.

The Trust may also be terminated by the Trustee on any prior date to when all Financial Assets forming part of the Trust Fund have been liquidated / realised, including by transfer of such Financial Assets to any other trust/scheme, in accordance with the terms of this Deed, subject to prior written consent of Security Receipt Holders holding at least 90% in value of the then outstanding Security Receipts issued pursuant to this Deed.

2.7.2 Upon termination of the Trust, the Trust Fund, including the proceeds of any liquidation/realisation of the Financial Assets, shall be distributed to the Security Receipt Holders, in the manner set out in Section 3.8 (*Payment Mechanism*) of this Deed and the Security Receipts held by the Security Receipt Holders shall stand extinguished, whether they have been fully redeemed or not. The Security Receipt Holders shall have no claim against the Trustee in this regard, including in respect of any unredeemed or unrealised portion of the Security Receipts, if any, except in the case of gross negligence, fraud, wilful misconduct or breach of the terms of this Deed by the Trustee or with respect to any accrued rights.

3.3 Control of Trust Fund

The Trustee shall in terms of the contractual arrangement in this Deed and the terms applicable to the Security Receipt Holders determine the extent of the application of the income of the Trust Fund and the distribution thereof.

3.4 Application of Trust Fund

The Trust Fund shall be absolutely applied for the purposes of the Trust in accordance with this Deed and the terms of the Security Receipts issued pursuant to this Deed, and shall not be applied, directly or indirectly, for any purpose or object otherwise than herein contained.

4 POWERS AND LIABILITIES OF THE TRUSTEE

4.1 Powers of Trustee

4.1.1 The Trust Fund shall vest in the Trustee, as a trustee in trust exclusively for the benefit of the Security Receipt Holders and the Trustee shall be absolutely vested with the general superintendence, direction and management of the affairs of the Trust and all powers, authorities and discretion appurtenant to or incidental to the purpose of the Trust, subject to the provisions of this Deed.

4.1.2 Without in any way limiting the generality of the powers, authorities and discretion conferred referred upon the Trustee under Section 4.1.1, the Trustee shall, subject to the relevant offer Document and in accordance with this Deed, have the following powers:

- (a) to accept Contributions ...
- (b) to acquire, sell, hold, manage, trade, lend and dispose of Financial Assets;
...
- (w) to vary, add or otherwise alter all or any of the features of the scheme contemplated under the relevant Offer Document and this deed with the prior written consent of the Security Receipt Holders representing not less than 90% in value of all the then outstanding security Receipts issued pursuant to this Deed;

...”

4.6 Duties of Trustee

...

4.6.6 The Trustee shall ensure that any amendment to this Deed shall be subject to the consent of the Security Receipt Holders representing not less than 90% in face value of all the then outstanding security Receipts issued pursuant to this Deed.

5.1 Contributions

...

5.1.2 Upon the making of the Contribution, each Security Receipt Holder shall be entitled to the undivided right, title and interest in the Trust Fund evidenced by the Security Receipts issued to it, on the terms and conditions contained in the Security Receipts and the relevant Offer Document.

5.2 Revocation of Contributions

5.2.1 The Security Receipt Holders shall be entitled to revoke the Contributions made by them, at any time during the term of this Deed, in accordance with the terms and conditions contained herein, for any reason, including but not limited to circumstances resulting from any adverse tax consequences (for either the Trust or the Security Receipt Holders) or any direction of any Statutory Authority, *provided that* no such revocation shall take effect unless the consent of the Security Receipt Holders holding Security Receipts representing not less than 75% of the total value of the then outstanding Security Receipts, issued pursuant to this Deed has been obtained, in this

behalf, provided that a notice of not less than 60 days of the intention to revoke the contribution is given to the Trustee.

5.2.2 In the event that the Trustee, at any time during the term of this Deed, faces any adverse tax consequences or upon any direction of any Statutory Authority, the Trustee shall have the right to call upon the Security Receipt Holders to revoke their Contributions if required as per applicable laws.

5.2.3 In the event that the Contributions are revoked in terms of this Section, the Trust Fund shall automatically stand transferred and shall automatically and without any further act, deed or writing, operate as an assignment vesting the Trust Fund jointly in favour of each of the Security Receipt Holders (in proportion to their Contributions) or to any Person designated by the Security Receipt Holders in this behalf *provided that* the Trustee has received payment of all Amounts Due or accrued to the Trustee in full, in accordance with the terms of this Deed. Upon such transfer all the provisions of the relevant Financing Documents and the Assignment Agreement shall apply *mutatis mutandis* to the Security Receipt Holders or their designee, and the Security Receipt Holders or their designee shall be entitled to all rights and remedies of the Trustee and shall be obliged to perform all its duties and obligations under the relevant Financing Documents and the Assignment Agreement, as if the Security Receipt Holders or their designee were party to the Financing Documents and the Assignment Agreement as of the date thereof.

5.5 Meeting of Security Receipt Holders

5.5.1 The Trustee may, at its discretion, or on a requisition of one or more of the Security Receipt Holders holding not less than 25% of the face value of all the then outstanding Security Receipts, issued pursuant to this Deed, convene a meeting of the Security Receipt Holders. ...

...

5.5.3 Any decision requiring the consent/ approval of the Security Receipt Holders shall be deemed to have been taken if the Security Receipt Holders holding not less than 75% of the face value of all the then outstanding Security Receipts, issued pursuant to this Deed, present and voting at such general meeting, vote in favour of such decision. *Provided that* any such decision requiring the consent and approval of the Security Receipt Holders may be obtained by a letter or letters, signed by the Security Receipt Holders holding not less than 75% of the face value of all the then outstanding Security Receipts, issued pursuant to this Deed, without convening a meeting of the Security Receipt Holders as if such letter or letters constitute a resolution passed or decision taken at a meeting duly convened and held as aforesaid and shall have effect accordingly.

5.5.4 Notwithstanding anything contrary contained in this Deed or any offer document issued pursuant to this deed, the majority of security holders holding not less than 75% of the face value of all the then outstanding Security Receipts will be entitled to call for meeting and advise resolution plan to Trustee, in case the trust assets are not liquidated or realised by the Trustee within the resolution period as may be extended as per RBI

Guidelines. Every resolution passed in such meeting shall be binding on the Trustee.

7.3 Removal of Trustee

At any time during the term of the Trust, the Trustee may be removed by a resolution of the Security Receipt Holders holding not less than 90% of the value of the then outstanding Security Receipts, issued pursuant to this Deed.

7.7 Breakage Costs

Upon any revocation of the Trust by the Security Receipt Holders pursuant to Section 5.2 (5.2 Revocation of Contributions) (other than a revocation of the Trust on account of adverse tax consequences) or upon any termination of the Trust by the Security Receipt Holders in accordance with this Section 7 or upon the appointment of any Person other than XYZ ARC as the Trustee in relation to the Trust, the investment manager and/or the asset management company, breakage costs of an amount mutually agreed upon, as determined for the purpose of the most recent declaration of the Net Asset Value shall be paid to the Trustee.

E. Service Provider Agreement dated 8th May 2019

ANNEXURE -A

The overall scope of the job of the Servicing Agent and the key accountabilities are listed below.

...

- (1) Company shall notify to AMC any settlements, compromises with the Borrowers or disposal of the Accounts allocated in exercise of powers conferred upon the Company under Collection Authority Matrix annexed in Annexure-C. Any settlement offer by Company to Borrower shall not require prior written approval from AMC. Company is free to do settlements, compromises with the Borrowers or disposal of the Accounts in any manner it deems fit without obtaining prior approval of AMC.

ANNEXURE - C

S No.	Activity	Maximum Limit	Approval Level
	Waiver in loan settlement	Upto Rs. 5 Lacs	2 Members from Level 1 & One Member from settlements Level 2 + CEO
		Above Rs. 5 Lacs	2 Members from Level 1 & One Member from settlements Level 2 + CEO + CEO of Holding Company

17. The Committee notes from the various documents provided by the querist that:

- The ABC Trust has been set up as a revocable trust requiring 75% majority to pass the resolution for dissolution of the Trust (clause 4.25.1 of Offer Document and 5.2.1 of Declaration of Trust).
- The Company, being a holder of 85% of SRs, can requisition and convene the meeting of SR holders at any time (clause 5.5.1 of Declaration of Trust).

- The Company being a holder of 85% of SRs is entitled to revoke the contributions made by it at any time during the term of the Trust Deed; and in such event, the Trust Fund (comprising mainly of loan receivables assigned to the Trust/Trustee) shall vest with the SR holders in proportion to their contributions and they shall be entitled to all the rights and remedies of the Trustee (clause 4.25.1 & 4.25.3 of Offer document).
- The return of the Company from the Security Receipts is entirely dependent on the monies received from the Assets of the Trust, which comprise of the amounts due from loan receivables, which have been assigned to the Trust/Trustee (clause 4.4 of the Offer document).
- The Company is exposed to all the credit risks and other risks from non-recovery of loan receivables and is also bearing all the risks even in relation to operation of the trust, such as, adverse tax consequences on the Trust, etc. (clause 4.26 of Offer document).
- The Trustee or the ARC is not exposed to any kind of risks from the loans receivable assigned; and is basically providing the services of securitization and asset reconstruction, earning fixed management fee & incentive for early redemption [clauses 6.4.1(d) and 6.4.1(e) respectively of Offer document].
- Whilst the XYZ AMC was to manage the assigned portfolio in terms of paragraph 6.12 of offer document, the management and recovery of the loans have been given to the Company in terms of Service provider agreement carrying fixed fee of 6% of the collection made.
- Even in case, the trust is prematurely dissolved as a result of revocation of contribution or if any other person is appointed as a trustee in place of XYZ ARC, the Trustee AMC has to be paid breakage fee and such amount to be determined at the time of revocation (clause 7.7 of Declaration of Trust).
- Settlement offer by Company (in regard to assigned debts) shall not require prior written approval from XYZ AMC and the Company is free to do settlements, compromises with the Borrowers or disposal of the Accounts in any manner it deems fit without obtaining prior approval of AMC (Annexure C of Service Provider Agreement).
- Trustee is only holding the Trust Fund comprising of loans receivables for the benefit of and in trust for SR holders, wherein 85% of the SRs belong to the Company.

18. From the above, the Committee is of the view that though there is an assignment in favour of a special purpose vehicle (ABC Trust), the Company, being the holder of 85% security receipts in the ABC Trust, continues to be exposed to substantially all the risks and rewards of ownership and also controls the SPV (ABC Trust) by virtue of the Company having more than requisite power necessary to revoke the SPV. The presence of joint control in respect of some of the items requiring approval of 90% of the voting power, for example, removal of trustees, is though relevant but does not alter the ability of the Company to liquidate the SPV and which will result in outstanding Security Receipts being substituted by the underlying loan receivable portfolio.

D. Opinion

19. On the basis of the above, the Committee is of the opinion that derecognition of the loan receivable portfolio in the extant case is not in consonance with the derecognition requirements, enunciated in Ind AS 109, 'Financial Instruments'.

1. Whether a document, manifestly reading like a transfer agreement, has the true effect of transferring an asset or is merely disguised funding transaction has always been a matter of contention. All is well in good times. But in times of distress, questions are raised as to whether the purported transaction is a sale or financing transaction. If the transaction is treated as financing transaction, the very purpose of sale documentation is frustrated.

2. The question of 'true sale' is, therefore, a question whether a documented sale will be regarded as truly achieving the objective of a sale, and will be respected as such in bankruptcy or similar situation. So, the transaction, inherently driven by financing motive but is structured as sale transaction. The motive is financing, the mechanism is selling. It is to be examined (a) whether the legal device of sale is so clear and defensible that the motive thereof becomes irrelevant, or (b) whether the underlying intent is so pervasive that the legal device is eclipsed. Whether the intention is to put the asset into the exclusive right of the buyer and therefore put the asset beyond the reach of the liquidator in the event of insolvency of the seller.

In number of structured finance transaction, the objective is to achieve bankruptcy remoteness. In the present context, the bankruptcy remoteness means to structure the transaction in such a manner that even if the entity (seller) goes into insolvency, the liquidator will not be able to reach out to the asset in question. For instance, if the transaction in question is securitization, the pool of assets has been 'sold' to the SPV. Can the liquidator question the sale and reclaim the ownership rights over the pool of assets? Can the liquidator give priority to the so-called investors in a securitization transaction only at par with other lenders? Whether the investors are prone to substantial hair-cuts? This explains the significance of the 'true sale' treatment.

In India, securitization or direct assignment transactions are guided by Guidelines on Securitization and Direct Assignment issued in 2012 by the Reserve Bank of India. As per the said Guidelines, the isolation of assets or 'true sale' from the originator to the SPV is an essential pre-requisite. An illustrative and inclusive list of criteria for true sale has been prescribed in 2006 RBI Guidelines as under:

- The selling bank / NBFC shall effectively transfer all risks / rewards and rights / obligations pertaining to the asset and shall not hold any beneficial interest in the asset after its sale except those specifically permitted under the guidelines.
- The buyer shall have the unfettered right to pledge, sell, transfer or exchange or otherwise dispose of the assets free of any restraining condition.
- The selling bank / NBFC shall not have any economic interest in the assets after its sale and the buyer shall have no recourse to the selling bank / NBFC for any expenses or losses except those specifically permitted under the said guidelines.
- There shall be no obligation on the selling bank / NBFC to re-purchase or fund the repayment of the asset or any part of it or substitute assets held by the buyer or provide additional assets to the buyer at any time except those arising out of breach of warranties or representations made at the time of sale.
- If the seller of loans acts as the servicing agent for the loans, it shall not detract from the 'true sale' nature of the transaction, provided such service obligations do not entail any residual credit risk on the sold assets or any additional liability for them beyond the contractual performance obligations in respect of such services.
- Any re-schedulement, restructuring or re-negotiation of the terms of the underlying agreement(s) effected after the transfer of assets to the buyer, shall be binding on the buyer and not on the selling bank / NBFC except to the extent of MRR.

The aforesaid transaction is now discussed in terms of Ind AS, the applicable GAAP also considering the aforesaid significance of 'true sale' as per the Guidelines on Securitization and

Direct Assignment issued by Reserve Bank of India. Ind AS 109 provides a detailed set of requirements for derecognition of all types of financial assets, be it a simple maturity of an instrument or a complex securitization transaction. The standard provides a flow chart to evaluate whether and to what extent a financial asset is recognized. Every transaction should be evaluated as per the strict sequence of the flow chart. Basically, there are two separate approaches to derecognition under Ind AS: the ‘risks & rewards’ approach and the ‘control approach’. First, the risk & rewards approach should be evaluated. If it fails to provide a clear answer the control approach should be applied.

3. The following flow chart, as per the application guidance, illustrates the evaluation of whether and to what extent a financial asset is derecognized:

Step		Description	Action	Decision
1		Consolidate all subsidiaries (Paragraph 3.2.1 of Ind AS 109)		
		↓		
2		Determine whether the derecognition principle below are applied to a part or all of an asset (or group of similar assets) (Paragraph 3.2.2 of Ind AS 109)		
		↓		
3		Have the right to the cash flows from the asset expired? (Paragraph 3.2.3(a) of Ind AS 109)	→ Yes	→ Derecognise the asset
		No		
		↓		
4	Yes	Has the entity transferred its rights to receive the cash flows from the asset? (Paragraph 3.2.4(a) of Ind AS 109)		
		No		
		↓		
5		Has the entity assumed an obligation to pay the cash flows from the asset that meets the condition in paragraph 3.2.5 of Ind AS 109? (Paragraph 3.2.4(b) of Ind AS 109)	→ No	→ Continue to recognise the asset
		Yes		
		↓		
6		Has the entity transferred substantially all risks and rewards? (Paragraph 3.2.6(a) of Ind AS 109)	→ Yes	→ Derecognise the asset
		No		
		↓		
7		Has the entity retained substantially all risks and rewards? (Paragraph 3.2.6(b) of Ind AS 109)	→ Yes	→ Continue to recognise the asset
		No		
		↓		
8		Has the entity retained control of the asset? (Paragraph 3.2.6(c) of Ind AS 109)	→ No	→ Derecognise the asset

		Yes ↓			
9		Continue to recognise the asset to the extent of the entity's continuing involvement			

4. Each of the steps are now discussed as follows:

(i) *Step 1: Consolidate all subsidiaries (Paragraph 3.2.1 of Ind AS 109)*

Many entities establish structured entities, trusts, etc. to acquire financial assets before these financial assets or a part thereof, are transferred to third party investors. The transfer to such structured entities might qualify as a legal sale. However, if the substance of the relationship between the transferor and the structured entity indicates that the transferor controls the structured entity, the transferor should consolidate the structured entity. The entities have to decide whether they are applying the derecognition at the consolidated level or the stand-alone level. If the derecognition is applied at the consolidated level, then the entity should first consolidate all subsidiaries including the structured entity. If not, then this point is not to be considered.

In the present context, the structured entity ABC Trust was declared by XYZ ARC as per the Indian Trusts Act, 1882, SARFAESI Act (Securitization and Reconstruction of Financial Assets and Enforcement of Security Interest Act, 2002) and applicable RBI guidelines vide deed dated 28th March 2019. The Trustee of the aforesaid Trust is also XYZ ARC. The Trustee as per the trust deed, particularly clause 4, has been vested with substantial powers over the relevant activities and has control over the Trust. On the contrary, the Company, as per the Trust Deed and other documents has no power over the Trust. It thus fails to satisfy the first criteria of control as per Ind AS 110, Consolidated Financial Statements. Thus, The Company is not required to consolidate the aforesaid Trust.

Further, the examination of derecognition is at stand-alone level.

It may also be mentioned that in certain clauses (Termination of Trust – clause 2.7.1; Power of Trustees – clauses 4.1.2 (a), 4.1.2(s), 4.1.2(w), 4.1.2 (bb) 4.1.2 (cc); Power to Delegate - clause 4.3; Duties of the Trustee – clause 6; Removal of Trustee – clause 7.3; Appointment of Trustee – clause 7.5.1) of the Trust Deed, it has been mentioned that the said clauses shall be operative only on agreement of security receipt holders representing not less than 90% in face value of the then outstanding security receipts issued pursuant to the Trust Deed.

The Company holds 85% of the security receipts issued by the Trust. An impression is created that without the explicit consent of the Company, the activities of the Trust cannot be conducted. In this context one should refer to substantive rights and protective rights as discussed in Ind AS 110, 'Consolidated Financial Statements'.

To have power over an investee, an investor must have existing rights that give it the current ability to direct the relevant activities. An investor's right over an investee can be either substantive or protective. For the purpose of assessing power, only substantive rights and the rights that are not protective shall be considered.

Substantive rights are those rights that an investor holds that give it the current ability to direct the investee's relevant activities. Substantive rights might arise through a combination of factors. For example, ownership of more than half of the voting rights would usually give an investor power, but the majority owner should also consider the existence of statutes, contractual agreements, board control, rights held by other parties,

and whether it has the practical ability to direct the investee's relevant activities. For a right to be substantive, the holder must have the practical ability to exercise that right. Another condition that must be met before rights are considered to be substantive is that the rights must be exercisable when decisions about the direction of the relevant activities need to be made.

Relevant activities are the activities of the investee that significantly affect the investee's return.

The relevant activities of Trust are mentioned in detail in clause 2.8 – 'Object of the Trust', in the Trust Deed. The objects include acquisition of loans and other financial assets, to carry on the activity of securitization and / or asset reconstruction, formulating strategies and taking all actions for recovery of amounts due and enhance the returns to security receipt holders and to take such action as may deemed to be necessary by the Trustees.

In short, the present relevant activities of the trust are to formulate strategies and take all actions for recovery and settlement of the loan portfolio. As per the Trust Deed, all these activities are to be carried out by the Trustee and in carrying out this act, the Trustee is not required to approach or obtain consent of the Company. The Company cannot direct the relevant activities. The Company cannot direct the Trustee to take certain actions.

It may be mentioned that XYZ ARC, the Trustee has appointed the Company as a resolution agent for collection / recovery of the loan portfolio vide Service Provider Agreement dated 8th May 2019 on payment of a collection fee. An agent is a party primarily engaged to act on behalf of and for the benefit of another party or parties and therefore does not control the investee when it exercises its decision making authority. Thus, sometimes a principal's power may be held exercisable by an agent, but on behalf of the principal. The service provider agreement clearly mentions that XYZ ARC, the trustee of the Trust is the principal and the Company is the agent. The existence of 'Service Provider Agreement' does not grant any substantive rights to the Company.

Protective rights are the rights designed to protect the interest of the party holding those rights without giving that party power over the entity to which those rights relate. An investor that has only protective rights will not control an investee. Protective rights are those that apply in exceptional circumstances or relate to fundamental changes in the investee. Protective rights are designed to protect the interests of the holder of such rights without giving that party power over the investee. Hence, an investor that holds only protective rights cannot have power, or prevent from another party from having power, over an investee. Example of protective rights includes the right of a lender to seize the assets of a borrower if the borrower fails to meet specified loan repayment conditions.

The clauses in the Trust Deed that require agreement of security receipt holders representing not less than 90% in face value of the then outstanding security receipts are protective in nature, which are operative only in certain exceptional circumstances to protect the interest of security holders. They do not bestow any power on the Company to control and direct the relevant activities. It is expected that the Company shall take rational decisions.

A simple analogy can be drawn from the Companies Act, 2013. Generally, an entity who holds equity interest in excess of 50% in another entity consolidates the second entity. The first entity can, ordinarily get all the ordinary resolution approved by the shareholders of the second entity. However, certain matters require special resolution of

the shareholders of the second entity and the first entity may not get all the matters that require special resolution approved in its favour. That does not preclude the first entity from consolidating the second entity as per accounting standards.

Thus, the Company has no power and hence, no control over the Trust. The Trust is controlled by XYZ ARC.

Conclusion: Therefore, this step is not to be considered for the present examination. One should now proceed to step 2.

(ii) *Step 2: Determine whether the derecognition principle below are applied to a part or all of an asset (or group of similar assets) (Paragraph 3.2.2 of Ind AS 109)*

The Company is a housing finance company that has given term loans, either housing or non-housing to various persons. These term loans have been further classified as standard assets, sub-standard assets, doubtful assets and loss assets as mandated by RBI. The loan assets classified as sub-standard assets, doubtful assets and loss assets are collectively referred as 'non-performing assets'. The Company, on 29th March 2019, vide Assignment Agreement assigned out of its non-performing assets, assigned in its entirety 243 term loan accounts of carrying value of Rs. 3038.13 lakhs to ABC Trust. The complete list is a part of the aforesaid assignment agreement.

Conclusion: The present examination of derecognition principle below is applied to and limited to these 243 term loan accounts of carrying value of Rs. 3038.13 lakhs and their entire cash flows.

(iii) *Step 3: Have the right to the cash flows from the asset expired? (Paragraph 3.2.3(a) of Ind AS 109)*

This step considers whether the contractual rights to the cash flows from the financial assets have expired. In case, the contractual rights have expired, the financial asset is derecognized.

In the normal course of business, a loan is extinguished by payment of the entire due amount. Therefore, because the borrower has discharged its obligation, the lender would derecognize the term loan account from that date. This is not the present case. Here, the borrower has defaulted in payment of entire dues.

The Company has granted these term loans over a period of last few years. The said parties however defaulted on the principle and other dues thereof. Unable to recover its dues, the Company has filed legal suits in courts for the recovery for all 243 term loan accounts. One of the important points of getting relief that the loan should not be barred for recovery as per the Limitation Act, 1963. The Limitation Act provides that every suit filed after the limitation shall be dismissed. Thus, if barred by limitation, recovery of loans cannot be proceeded with through court of laws. The recovery suit has to be filed within the limitation period. The Company has represented that all the recovery suits in these 243 term loan accounts have been filed within the limitation period. It should be noted that as per Ind AS 109, the Company has recognized a provision of expected credit loss on these amounts at Rs. 856.31 lakhs.

Conclusion: It is understood that the contractual rights to receive cash flows from the said 243 loan accounts have not expired. Thus, they cannot be derecognized at this step.

(iv) *Step 4: Has the entity transferred its rights to receive the cash flows from the asset? (Paragraph 3.2.4(a) of Ind AS 109)*

If the contractual rights to the cash flows have not expired, an entity assesses if it transfers the cash flow from the asset. Ind AS 109 does not explain what is meant by the phrase '*transfers the contractual rights to receive the cash flows of the financial asset*'. The implication is that a transfer occurs when the cash flows from an asset are legally sold or assigned. The term debt assignment refers to the transfer of debt, and all the associated rights and obligations, from a creditor to a third party. Vide Assignment Agreement dated 29th March 2019, the Company in its capacity as the Assignor assigned to ABC Trust, the said 243 loans of carrying value of Rs. 3038.13 lakhs disbursed under various financing documents together with all its rights, title and interest including underlying security interest, pledges and/or guarantees in respect of such loans. The Company has also obtained a legal opinion which has been submitted by the querist for the perusal of the Committee.

The relevant extract is as under:

'The assignment of the receivables by the Assignor to the Assignee in the manner contemplated in the transaction documents will constitute an absolute assignment and transfer (ie a sale or true sale) and will convey to the Assignee a legally enforceable right in the debts/actionable claims assigned to it. In this context please note that there are no statutory or regulatory provisions in India which set out the basis for determining whether a direct assignment transaction satisfies the requirement of true sale. The principle to determine true sale have evolved on the basis of case law which has specified the aspects of transaction that could have an impact on true sale. These include inter alia features of the transaction, which provide that the entire risk and rewards in respect of the transaction would not arise to the assignee, following the transfer. Further, the term 'true sale' has not been defined under Indian law other than the criteria prescribed for 'true sale' under the Guidelines on Transactions Involving Transfer of Assets through Direct Assignment of Cash Flows and the underlying securities issued by the Reserve Bank of India on May 7, 2012 (Securitization Guidelines). Accordingly, the criteria for true sale as set out have been arrived at on the basis of general legal principles by the Courts of law in respect of a sale transaction'.

As per the aforesaid RBI guidelines, the criteria of true sale are as under:

- The 'sale' (this term would hereinafter include direct sale, assignment and any other form of transfer of asset, but does not include bills rediscounted, outright transfer of loan accounts to other financial entities at the instance of the borrower and sale of bonds other than those in the nature of advance) should result in immediate legal separation of the 'selling NBFC' (this term hereinafter would include direct selling NBFC, assigning NBFC and the NBFC transferring assets through any other mode), from the assets which are sold. The assets should stand completely isolated from the selling NBFC, after its transfer to the buyer, i.e., put beyond the selling NBFC's as well as its creditors' reach, even in the event of bankruptcy of the selling/assigning/transferring NBFC.
- The selling NBFC should effectively transfer all risks/rewards and rights/obligations pertaining to the asset and shall not hold any beneficial interest in the asset after its sale except those specifically permitted under these guidelines. The buyer should have the unfettered right to pledge, sell, transfer or exchange or otherwise dispose of the assets free of any restraining condition. The selling NBFC shall not have any economic interest in the assets after its sale and the buyer shall have no recourse to the selling NBFC for any expenses or losses except those specifically permitted under these guidelines.
- There shall be no obligation on the selling NBFC to re-purchase or fund the

repayment of the asset or any part of it or substitute assets held by the buyer or provide additional assets to the buyer at any time except those arising out of breach of warranties or representations made at the time of sale. The selling NBFC should be able to demonstrate that a notice to this effect has been given to the buyer and that the buyer has acknowledged the absence of such obligation.

- The selling NBFC should be able to demonstrate that it has taken all reasonable precautions to ensure that it is not obliged, nor will feel impelled, to support any losses suffered by the buyer.
- The sale shall be only on cash basis and the consideration shall be received not later than at the time of transfer of assets. The sale consideration should be market-based and arrived at in a transparent manner on an arm's length basis.
- If the seller of loans acts as the servicing agent for the loans, it would not detract from the 'true sale' nature of the transaction, provided such service obligations do not entail any residual credit risk on the sold assets or any additional liability for them beyond the contractual performance obligations in respect of such services.
- An opinion from the selling NBFC's Legal Counsel should be kept on record signifying that : (i) all rights, titles, interests and benefits in the assets have been transferred to the buyer; (ii) selling NBFC is not liable to the buyer in any way with regard to these assets other than the servicing obligations as indicated in paragraph 2.5.6 above; and (iii) creditors of the selling NBFC do not have any right in any way with regard to these assets even in case of bankruptcy of the selling NBFC.
- Any re-schedulement, restructuring or re-negotiation of the terms of the underlying agreement/s effected after the transfer of assets to the buyer, shall be binding on the buyer and not on the selling NBFC except to the extent of MRR.
- The transfer of assets from selling NBFC must not contravene the terms and conditions of any underlying agreement governing the assets and all necessary consents from obligors (including from third parties, where necessary) should have been obtained.

In case the selling NBFC also provides servicing of assets after the sale under a separate servicing agreement for fee, and the payments/repayments from the borrowers are routed through it, it shall be under no obligation to remit funds to the buyer unless and until these are received from the borrowers.

Conclusion: As per the above discussion and on a perusal of Assignment Agreement dated 29th March 2019, and RBI guidelines it can be concluded that the Company has transferred its rights to receive the cash flows of the said 243 term loan accounts, being non-performing assets as per prudential norms of RBI, of carrying value of Rs. 3038.13 lakhs (against which the Company has created a provision of Rs. 856.31 lakhs being expected credit loss) at a total lumpsum consideration of Rs. 2,278.60 lakhs to ABC Trust of which XYZ ARC is the trustee vide aforesaid assignment agreement.

(v) *Step 5: Has the entity assumed an obligation to pay the cash flows from the asset that meets the condition in paragraph 3.2.5 of Ind AS 109? (Paragraph 3.2.4(b) of Ind AS 109)*

As per the Assignment Agreement dated 29th March 2019, the assignment of term loan accounts in favor of ABC Trust is absolute. The responsibility of collection of cash flows is that of the Trust. The Company has assumed no obligation to collect the cash flows from these loans receivables and then pay the cash flows to the Trust. The cash flows have to be collected by the Trust.

Conclusion: This step is not applicable to the present transaction and hence skipped.

Once an entity has established that it has transferred a financial asset, either by transferring the contractual rights to receive the cash flows or under a qualifying pass-through arrangement, it carries out the risks and rewards test. This test requires the entity to evaluate whether it has:

- Transferred substantially all the financial asset’s risks and rewards of ownership;
- Retained substantially all the risks and rewards of ownership; or
- Neither transferred nor retained substantially all the risks and rewards of ownership. If this is the case, the entity should perform a control analysis to ascertain which party has control of the asset.

The aforesaid discussion can be illustrated as under:

More risks and rewards transferred from transferor to transferee	Situation		Accounting treatment for transferor
	Substantially all risks and rewards transferred		Derecognize transferred asset. Recognize any new assets / liabilities.
	Neither retained nor transferred substantially all risks and rewards of ownership	Control no longer retained by transferor – transferee can unilaterally sell the transferred asset	
		Control retained by transferor – transferee cannot unilaterally sell the transferred asset	Recognize asset and liability to the extent of continued involvement
	Substantially all risks and rewards retained		Continue to recognize transferred asset. Proceeds from transfer are recognized as a financial liability

(vi) *Step 6: Has the entity transferred substantially all risks and rewards? (Paragraph 3.2.6(a) of Ind AS 109)*

There is no ‘bright line’ provided in Ind AS 109 as to what is meant by a transfer of ‘substantially all’ of the risks and rewards of ownership, and a significant degree of judgement is required when applying the risks and rewards test.

Typical risks included in a risk and reward analysis are interest rate risk, credit risk (risk of default) and late payment risks.

The transfer of substantially all the risks and rewards of ownership is generally apparent from the terms and conditions of transfer. If the transfer is not obvious, the entity needs to compare the exposure to the variability in the present value of the transferred asset’s future net cash flows before and after the transfer. The computation and comparison should be made using an appropriate current market rate as the discount rate. All reasonable possible variability in net cash flows (as to amount and timing) should be considered. The amounts and timing of cash flows should be probability weighed.

The flow of the present transaction is as under:

- Declaration of ABC Trust on 28th March 2019;
- Issuance of Offer Document dated 29th March 2019 by the Trust for issuance of Security Receipt (SR) of Rs. 2278.60 lakhs;
- Allotment of SR by the Trust on 29th March 2019 in the ratio of 85:15 to the Company (Rs. 1936.81 lakhs) and XYZ ARC Limited (Rs. 341.79 lakhs);

- Assignment of loans receivables of Rs. 3038.13 lakhs by the Company to the Trust by Assignment Agreement dated 29th March 2019.

The following data should also be referred to:

Number of loan receivable accounts (1)(2)	243 cases
Litigation against (2)	All 243 cases
Principal Outstanding (1) & recognized in books	Rs. 3038.13 lakhs
Total Outstanding as on 26.03.2019(1) Recognized in books – Rs. 3038.13 lakhs	Rs. 3934.64 lakhs
Value of security there against(1)	Rs. 5958.18 lakhs
Sale consideration received by the Company	Rs. 2278.60 lakhs
ECL provision by Company	Rs. 856.31 lakhs
Face value of SRs held by the Company	Rs. 1936.81 lakhs
Notes:	
1. As per XYZ ARC bid dated 29.03.2019	
2. As per Assignment Agreement dated 29.03.2019	

From a business perspective against the dues of Rs. 3934.64 lakhs, the value of security is Rs. 5958.18 lakhs. It is true that litigation is pending in all these cases and the resolution may take several years. To reduce the litigation period and early recovery of cases, the SARFAESI Act has been promulgated that gives additional powers of recovery to the ARCs. Through the securitization methodology it is expected that recovery / resolution of loan receivables shall be higher in terms of amount and much faster in terms of timing. It can be said that the present value of cash flows could be higher under this methodology when compared with a situation where the Company had continued to hold the loans receivables in its book and had not assigned them to the Trust.

An argument can be advanced that substantial risks & rewards have not been transferred in the present case as these have now been embedded in the SRs which have been issued in lieu of loans receivables. The Trust is a special purpose vehicle and its assets consist only the aforesaid loan receivables. The distribution / redemption of SRs is based solely on the realization of the aforesaid loan receivables.

However, the flow of the transaction depicts a different picture. First the SRs were issued in cash by the Trust which then utilized the proceeds to acquire the loan receivables in cash. It is not the case where loans receivables have been acquired first and then, SRs have been issued as a part consideration.

The issuance of SRs and assignment of loan receivables are 2 separate transactions and should not be clubbed together. They should be treated separately.

Further, paragraph B3.2.4 of Ind AS 109 provides examples of when an entity has transferred substantially all the risks and rewards of the ownership. These 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).

In the present matter, it is obvious that examples b and c are not applicable. Example a can be applied as the assignment is absolutely unconditional. On perusal of the

Assignment Agreement, this is clearly a case of an unconditional sale of financial asset. The Company or the Trust has not attached any condition to the assignment of loan portfolio except normal covenants and warranties. The assignment cannot be revoked by either of the parties. It may be argued that redemption of security receipts are dependent on realization of loan portfolio, but that does not make the sale conditional. The assignment cannot be rolled back.

Conclusion: It can be concluded having regard to the above discussion, more particularly, the examples in paragraph B3.2.4 of Ind AS 109, that substantially all the risks and rewards of the ownership of loans receivables have been transferred.

(vii) *Step 7: Has the entity retained substantially all risks and rewards? (Paragraph 3.2.6(b) of Ind AS 109)*

In view of conclusion reached in step 6, the discussions under this step are primarily academic in nature.

The comparability of the variability of the transferred asset's cash flows before and after the transfer might show that the entity's exposure to the variability does not change significantly as a result of the transfer. The entity is regarded as having retained substantially all the risks and rewards of the asset's ownership. It should continue to recognize the asset.

As per paragraph B3.2.5 of Ind AS 109, the following are the examples where an entity has retained substantially all the risks and rewards of ownership:

- 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.

If one considers and appreciates the aforesaid examples, the present transaction does not compare even remotely to any of the aforesaid examples. The Company has no recourse to the assigned loan receivables. It has not given any warranty with respect to any of the loans receivables. Having assigned, it has no role to play in the realisability of the loans receivables. It may however be mentioned that its realisability/ redemption of SRs is dependent upon the recoverability of loan portfolio. But as far as assigned assets are concerned, the Company has no rights whatsoever.

Here again, it can be argued that the Company is the major security receipt holder in the Trust but it has very limited powers. As discussed above, at most it has protective rights with certain limited and exceptional matters. The substantial rights to direct the relevant activities of realisation of loan portfolio vests with XYZ ARC.

Conclusion: It can be concluded that the Company has not retained any risks & rewards of the assigned assets.

(viii) *Step 8: Has the entity retained control of the asset? (Paragraph 3.2.6(c) of Ind AS 109)*

An entity (transferor) that has retained some risks and rewards, but not substantially all of them, is in the middle ground in which the risks and rewards analysis does not provide a clear answer. The transferor then has to determine whether it has retained control of the asset:

- a. If the transferor has not retained control, it must derecognize the financial asset and recognize separately, as assets or liabilities, any rights and obligations created or retained in the transfer;
- b. If the entity has retained control, it must continue to recognize the financial asset to the extent of its continuing involvement in the financial asset.

(Ind AS 109, paragraph 3.2.6(c))

Control is based on whether the transferee has the practical ability to sell the transferred asset. Control, in this context, does not have the same meaning as in Ind AS 110.

The ability to sell a transferred asset looks to what the transferee, and not the transferor, can do with the asset. If the transferee has the practical ability to sell the transferred asset, it has control over the asset. If the transferee does not have the practical ability to sell the transferred asset, the transferor has retained control of the transferred asset.

The transferee has the ‘practical ability’ to sell the transferred asset if:

- a. It can sell the asset in its entirety to an unrelated third party; and
- b. It is able to exercise that ability unilaterally and without imposing additional restrictions.

(Ind AS 109, paragraph 3.2.9)

These conditions should be evaluated by considering what the transferee is able to do in practice, and not what contractual rights it has with respect to the transferred asset.

(Ind AS 109, paragraph B3.2.8)

The transferee might have a contractual right to dispose of the transferred asset. That right will have little practical effect if there is no market for the transferred asset.

(Ind AS 109, paragraph B3.2.8(a))

The transferee should also be able to exercise its ability to transfer the asset independently of the action of others. The transferor should not impose additional restrictions or strings to the transfer (eg conditions about how a loan asset is serviced or an option giving the transferee the right to repurchase the asset).

(Ind AS 109, paragraph B3.2.8(b)(i)).

To examine ‘control’ as per above, the following documents were perused:

- a. Declaration of ABC Trust deed dated 28th March 2019;
- b. Assignment Agreement dated 29th March 2019 between the Company and XYZ ARC;
- c. Security Receipts (SRs) Offer Document issued by ABC Trust dated 29th March 2019.

One couldn’t come across any term, condition, clause or paragraph that would negate any of the control tests as mentioned above. The Trust has the unilateral power to deal with or dispose of the loan receivables. The Company has no power or right to intervene in any manner. Clause 4.1.2(b) provides power to the trustee ‘to acquire, sell, hold, manage, trade, lend and dispose of Financial Assets’ without any restrictions or strings.

Similar powers are given as per clause 4.1.2(h) of the Trust Deed. However, attention is invited to clause 4.1.(cc) of the Trust Deed that states: that the Trustee shall have the power ‘to transfer or exchange all or any of the Financial Assets forming a part of the Trust Fund between the various schemes / trusts established by XYZ ARC or to or with any other person, at the sole discretion of Trustee and in accordance with the Transaction Documents, provided that such transfer or exchange shall be at least at the value of the Financial Asset, as calculated to determine the prevailing Net Asset Value and provided further that the prior written consent of the Security Receipt Holders representing not less than 90% in value of all the then Security Receipts issued pursuant to this Deed shall have been obtained’. It may be argued that this clause places restrictions on the powers of the Trustee as the transaction requires consent on not less than 90% of the Security Receipt holders. Thus, without the consent of the Company, who holds 85% of Security Receipts, the Trustee cannot sell or exchange the Financial Assets. This interpretation is not correct. The clause has to be read in conjunction with the ‘Transaction Documents’ including the assignment agreement when the Company is involved (the Company has substitution rights and can always transfer its security receipts to a third party). As per clause 2 of the assignment agreement, the Company has unconditionally and irrevocably sold, assigned, transferred and released to and unto the Trust all the loans with the intent that the Trust shall be the full and absolute legal owner and only person legally entitled to the loans. The Company has also agreed in the assignment agreement to execute such further documents as may be necessary for the purpose of aforesaid agreement. As per clause 6.2 of the assignment agreement, the Trust shall have the sole right of collecting any monies pertaining to the loans including the amounts due, enforcing the underlying security interests, pledges and / or guarantees and enforcing payment of all the loans, in whatever manner it may consider necessary and prudent, in its absolute discretion.

The Trustee has unfettered right to deal with the financial assets as per clause 4.1.2(d). Then why this clause? The aforesaid clause 4.1.2 (cc) is a ‘safeguard’ clause to protect the interest of the security receipt holders. As per this clause, the Trustees have the discretion to transfer or exchange the Trust’s financial asset between the various trusts / schemes established by XYZ ARC (Trustee itself) or by any other person. Thus, there could be a direct or indirect related party transaction considering the ejusdem generis rule of interpretation of statutes. To ensure that no mischief occurs, two safeguards are inbuilt. One, the transaction value should not be below the net asset value. Second, approval is obtained so that the security holders could ensure protection of their rights. Further, this clause will generally be operative only in exception circumstances. The security receipt holders are expected to be rational. The aforesaid clause cannot be stretched and interpreted to mean that this casts a threat to the practical ability on the Trust to deal with the financial assets or there are strings attached. The beneficial and harmonious rules of interpretation of statutes are applicable. Otherwise clause 4.1.2(b) and clause 4.1.2(h) becomes redundant and that obviously cannot be the objective of the Trust.

For the purpose of this Transaction, the Assignment Agreement is paramount. It has to be seen whether any strings are attached therein.

Conclusion: It can be concluded that the control of the loan receivables vests absolutely with the Trust. None of the control aspects has been retained by the Company. The Company can derecognize the loan receivables from its books of accounts.

(ix) *Step 9: Continue to recognize the asset to the extent of the entity’s continuing involvement*

The continuing involvement approach applies if the entity has:

- Not transferred or retained substantially all the risks and rewards of ownership;
and
- Control has not passed to the transferee.

In such a scenario, the entity continues to recognize part of the asset under the continuing involvement approach. That part represents the extent of its continuing exposure to the risks and rewards of the financial asset.

Ind AS 109, paragraph 3.2.16

As discussed above, the Company has transferred and not retained substantially all the risks and rewards of ownership; and control has passed to the Trust, there is no continuing involvement of the Company. Thus, the asset has to be derecognized in its entirety.

Conclusion: As discussed above, the Company has transferred and not retained any risks and rewards of ownership; and control has passed to the Trust, there is no continuing involvement of the Company. Thus, the asset has to be derecognized in its entirety.

Overall Conclusion of the Querist:

Based on the aforesaid analysis and discussion, the Company has correctly derecognized the loan portfolio and recognized the SRs as Investments as per the applicable provisions of Ind AS particularly Ind AS 109, 'Financial Instruments'.
