

Query No. 3

Subject: Treatment of Investments in Subsidiaries/Associates held through Policyholders' Funds.¹

A. Facts of the Case

1. A Corporation (hereinafter referred to as 'the Corporation') is a statutory corporation established under the Act of Parliament and is engaged in the business of life insurance in and outside India. The Corporation is governed by the provisions of the Act under which it is formed and notifications thereunder (the Governing Act); it is also registered with the Insurance Regulatory and Development Authority of India (IRDAI) and is subject to such provisions of IRDAI Act and regulations thereunder which are not inconsistent with the provisions of the Corporation's Governing Act.

2. The Corporation prepares its standalone annual financial statements in the format prescribed under the Governing Act as also under IRDAI (Preparation of Financial Statements and Auditors' Report of Insurance Companies) Regulations, 2002 (IRDAI FS Regulations) and as per the applicable framework of Accounting Standards (AS) issued by the Institute of Chartered Accountants of India (ICAI). The Corporation is considering preparing and presenting Consolidated Financial Statements (CFS) under the provisions of applicable AS (i.e., AS 21) and other applicable Accounting Standards.

3. Prior to the enactment of Insurance Regulatory and Development Authority Act, 1999 (IRDA Act), the Corporation was governed by the provisions of Insurance Act, 1938 (the Insurance Act) and its Governing Act. The Corporation was operating as a corporation having a Single Fund. The bifurcation between policyholders' and shareholders' funds, as also bifurcation amongst policyholder of participating and non-participating bifurcation was not maintained for financial reporting purposes. In Pre-IRDAI period, some investments were made in group and other entities out of the said single fund. In the Post IRDAI period, the Corporation segregated the Shareholders and Policyholders funds in 2002 and few investments in group companies were allocated to Policyholders funds in the bifurcation done then. In Post-IRDAI period, the Corporation complies with the IRDAI Investment Regulations for all investments made subsequently, except for some specific investments out of policyholders' fund with specific dispensations from the Regulator.

4. The IRDAI FS Regulations, *inter alia*, require insurers to prepare and present annually (i) 'Revenue Account' also known as Policyholders' Account, (ii) Profit & Loss Account (also known as Shareholders' Account), (iii) Balance Sheet, (iv) Receipt and Payment Account or cash flow statement and (v) notes including significant accounting policies. In the Balance Sheet, on 'Asset' side, the investments are shown under three schedules i.e., Schedule 8 "Shareholders' Investments", Schedule 8A "Policyholders' Investments (Non-linked)" and Schedule 8B "Policyholders' Investments (Linked)".

¹ Opinion finalised by the Committee on 3.4.2021.

5. The Corporation as mentioned above, in course of its business as a life insurer, invests in various class of securities, including equity shares in other entities. The investments are made either from funds earmarked as 'Policyholders' fund' or from 'Shareholders' fund and are governed/regulated by Investment Regulations issued by IRDAI.

6. The Corporation, apart from holding investments in its subsidiaries and associates from its Shareholders' (SH) funds, has also allocated certain investments in some of its subsidiary and associates from its Policyholders' (PH) funds based on availability of funds. The investments from PH funds are generally made with a view to generate adequate periodic returns/gains therefrom so as to protect the interest of PH and to provide required liquidity for meeting claims, surrenders and other obligations on the life insurance policies written. These investments from PH Funds are broadly in nature of regulatory ring-fenced structure, being subject to several regulatory limits/conditions and are required to be maintained separately from SH Funds under the provisions of applicable law and regulations. In the balance sheet of the Corporation, PH funds are shown as liabilities' whereas SH funds represent equity.

7. The querist has stated that management of the Corporation proposes to prepare and present the Consolidated Financial Statements (CFS) under the framework of applicable Accounting Standards. The IRDAI FS Regulations or other rules/regulations of IRDAI do not provide any guidance pertaining to CFS; the technical material and provisions of applicable accounting standards also do not contain any specific guidance about consolidating the investments made through and held in PH funds.

8. The management of the Corporation evaluated the requirements of covering such of its Investments as are held in PH Funds while preparing the CFS under the applicable provisions of AS 21 or of AS 23; CFS are normally understood to be made and presented from the Group's owners' perspectives; whereas the Investments held in PH funds are not viewed as those of SHs or belonging to the owners, rather these are considered to be and shown as liabilities in the Balance Sheet of the Corporation.

9. For the investment made either from PH fund or SH fund, the rights, and obligations w.r.t. that investment is to be always borne by the insurance company (i.e., ultimately by the SH). For investments made from PH funds, the rights belong to PHs and for the obligations, if at all, at segment level shall be borne by SHs. For instance, if a deficit is created due to diminution in the fair value change of investment made in debenture instrument from PH fund impacting the solvency ratio, this deficit is required to be made good by the SH.

10. The insurance companies participate and engage with managements of investee company in capacity of owner of the investments held and not merely as a custodian of PH. There is no distinction in that sense being made as investment forming part of PH or that of SH.

11. As per the report of K P Narasimhan Committee (2005), the legislation requires the bifurcation of liabilities into PH funds and SH funds and envisages that PH fund is effectively held in trust for the benefit of the policyholders and that those exist to pay out benefits when the policies eventually result into claim or are surrendered. The income/gain or loss on investments held in PH funds are also accounted as part of the PH Funds (i.e., in the Revenue Account and not in Profit & Loss Account of the Corporation).

12. The regulatory requirement to maintain separate accounts is not merely to facilitate identification of investment held from PH funds or monies of the PHs but also to demonstrate that such funds are liability of the Corporation. The separation enables transferring the benefits accrued from such investments to the PHs, hence, to facilitate identifying the liabilities explicitly and to be treated as security to meet the obligations arising on account of policy contracts.

13. The Corporation (owners or SH) does not derive economic benefits emanating from investments in PH funds except for the Surplus, as worked out under regulatory provisions, therefrom at portfolio level after fully reserving based on actuarial valuation of the liabilities from all insurance contracts. Specified percentage of such surplus at the reporting date gets credited to SH Funds, as per the provisions of section 28 of the LIC Act. The economic benefits like dividend, interest or profits/gains of Investments in PH fund belong to and are accounted for as part of PH Funds.

14. According to the querist, an important aspect to be considered in the extant issue is whether the Corporation (its owners or SH) exercises control over the PH funds, which are presented as 'Liability' in the financial statements of the Corporation. In absence of deriving direct economic benefits from investments out of such PH funds, as stated in paragraph 13 above, these funds and investments out of that are not controlled by the SH or owners of the Corporation; instead, these funds are merely managed by the Corporation on behalf of the PH in fiduciary capacity only.

15. A view emerged within the management of the Corporation as to whether it is exercising control over the PH funds or not in view of the fact that PH Funds are presented as 'liability' in the financial statements of the Corporation. Further question as to whether economic benefits accrue to the Corporation from investments made and held in PH funds is also debatable, considering the definition of 'asset' as per the Framework for Preparation and Presentation of Financial statements, i.e., *a resource controlled as a result of past events from which future economic benefits are expected to flow* (emphasis supplied by the querist). As per the querist, as discussed above, no direct economic benefits flow to SH of the Corporation out of investments held through PH fund. Moreover, having regard to the constraints in transfer of funds by life insurance companies under the applicable sectoral regulations, investment in PH is not to be considered for consolidation.

16. The querist has further stated in 2019, the Corporation has acquired 51% stake in ABC Bank Limited (Investee Bank). The investment in the Investee Bank was made from PH fund. The investments from PH fund are made to obtain sufficient returns for policyholders and are made with an objective to exit at appropriate time.

17. Prior to acquisition of stake in the Investee Bank, necessary approval from IRDAI was sought. While granting the approval for the said acquisition, IRDAI had put certain conditions subject to which such Investment was made. The relevant conditions imposed by the IRDAI are summarised below:

- The Corporation shall ensure that acquiring additional stake in the Investee Bank is done in a prudent manner such that the interests of the policyholders are safeguarded.
- The Corporation shall make all efforts to maximise returns from the deal so that the returns are commensurate to the average returns from overall investments of the querist.
- The Corporation shall progressively bring down the stake in Investee Bank within the Regulatory limits as mandated by IRDAI (Investment) Regulations, 2016 (i.e., within 15% of the outstanding equity share capital (face value) of the investee bank) over a period of time as may be stipulated by the IRDAI

18. Further in September 2020, IRDAI communicated that it has fixed a 6-year timeframe from the date of acquisition of 51% stake in the Investee Bank, for the Corporation to bring its stake within the regulatory limits.

19. Approval conditions stipulated by IRDAI, being in nature of restrictive covenants, the Board of the Corporation contemplated that the stake acquired in the Investee Bank should be gradually disinvested at the earliest permissible timeline, considering the interest of the policyholders. Accordingly, the Board of the Corporation at its meeting held in November 2020 discussed and decided the roadmap for reducing the stake in the Investee Bank within 15% i.e., maximum permissible limit under the IRDAI Investment Regulations. The summary of such roadmap is as under:

- (i) Encouraging Investee Bank to raise capital from other sources, thereby bringing down the dependency on the Corporation to provide capital. [The stake of the Corporation, currently has already been reduced to 49.24% in this manner.]
- (ii) If Investee Bank is able to find alternate sources of funding, Corporation's stake in Investee Bank would be automatically reduced due to expansion of the base, over a period of time.
- (iii) Under conducive market conditions, the Corporation could sell some of its stake in Investee Bank.

20. In the process of evaluating the provisions of applicable Accounting Standards pertaining to Consolidation (i.e., AS 21), the querist has reproduced the relevant extracts from paragraph 11 of AS 21 as below:

“A subsidiary should be excluded from consolidation when:

- (a) control is intended to be temporary because the subsidiary is acquired and held exclusively with a view to its subsequent disposal in the near future; or
- (b) it operates under severe long-term restrictions which significantly impair its ability to transfer funds to the parent.

As per explanation (a) to paragraph 11 of AS 21, “where an enterprise owns majority of voting power by virtue of ownership of the shares of another enterprise and all the shares are held as ‘stock-in-trade’ and are acquired and held exclusively with a view to their

subsequent disposal in the near future, the control by the first mentioned enterprises is considered to be temporary within the meaning of paragraph 11(a)”.

Explanation (b) to paragraph 11 of AS 21 further states that “the period of time, which is considered as near future for the purposes of this Standard primarily depends on the facts and circumstances of each case. However, ordinarily, the meaning of the words ‘near future’ is considered as not more than twelve months from acquisition of relevant investments unless a longer period can be justified on the basis of facts and circumstances of the case. The intention with regard to disposal of the relevant investment is considered at the time of acquisition of the investment. Accordingly, if the relevant investment is acquired without an intention to its subsequent disposal in near future, and subsequently, it is decided to dispose off the investments, such an investment is not excluded from consolidation, until the investment is actually disposed off. Conversely, if the relevant investment is acquired with an intention to its subsequent disposal in near future, but due to some valid reasons, it could not be disposed off within that period, the same will continue to be excluded from consolidation, provided there is no change in the intention.”

21. The Corporation being statutory corporation established under the Act of Parliament engaged in the business of life insurance, provisions of the Governing Act mandate the Corporation to confine its operations to life insurance business and only such other businesses which are in connection with its said business.

22. The basic objective of any investments made from the PH fund is to provide returns. IRDAI directive also envisages that the Corporation shall make all efforts to maximize returns from the acquisition of stake in Investee Bank so that the returns are commensurate with the average returns from overall investment of the Corporation under the said fund.

23. Pre-approval of IRDAI specifically mandated the Corporation to progressively bring down the stake in Investee Bank within the Regulatory limits as mandated by IRDAI (Investment) Regulations, 2016 [i.e., within 15% of the outstanding equity share capital (face value) of the investee bank] over a period of time as may be prescribed, which was subsequently prescribed by IRDAI to be 6 years from the date of investment. Along with such gradual reduction in shareholding, the Corporation's control over the composition of Board of Directors of the Investee Bank would also correspondingly reduce. Hence, IRDAI approval for investment was subject to pre-conditions to dispose it within defined time period. Considering the size of investment and with an objective to maximise return for Policyholders, sufficient time period is given by the Regulator for disposal of investment. Irrespective of having such a stringent regulatory requirement, the Board of Corporation decided to invest, which clearly indicates the intent of the Corporation to dispose-off such investment at earliest possible opportunity. Such investments made by regulated entities in the given facts and circumstances need to be considered differently while interpreting the term 'near future'.

24. As per the intent at the time of making the said investment, in November 2019 the Board of the Corporation has framed a plan for gradual reduction of its stake in the investee bank.

25. The explanation to paragraph 11 of AS 21, takes cognizance of the nuances emanating for investments which are highly regulated and governed by the special framework. As can be noticed from explanation (b) above, “held for disposal in near future” is a relative term requiring to be interpreted in the light of given facts and circumstances. The said explanation recognises the fact that period of several years may also be considered to be “near future” on the basis of facts and circumstances of the case.

26. Considering the above, a view within the management of the Corporation emerged that the investment from PH fund in Investee Bank with binding pre-conditions from IRDAI was made exclusively with a view to dispose-off in the near future, hence, control is considered ‘temporary’.

B. Query

27. In view of the above, the querist has sought the opinion of the Expert Advisory Committee on the following issues:

- (i) Whether the investment made through and held in PH funds qualify to be consolidated/equity accounted in the consolidated financial statements of the Corporation.
- (ii) If the response to (i) is that the investments held through PH Funds is to be considered for consolidation/equity accounting, whether in the given facts and circumstances of the matter, the control held by the Corporation in the extant case can be considered as ‘intended to be temporary because the subsidiary is acquired and held exclusively with a view to its subsequent disposal in the near future’ as mentioned in paragraph 11(a) of AS 21 and therefore to be excluded from consolidation.
- (iii) If, the financial information of the Investee Bank is excluded from the consolidation:
 - (a) As per paragraph 11 of AS 21, investment in Investee Bank should be accounted for in accordance with Accounting Standard (AS) 13, ‘Accounting for Investments’ in the consolidated financial statements. However, paragraph 2 (c) of AS 13 states that "this standard does not deal with investments of retirement benefit plans and life insurance enterprises".
 - (b) The financial statements of the Corporation are prepared as per the IRDAI FS Regulations and Circulars issued thereafter and as per provisions of the Insurance Act, 1938, as amended from time to time. Part 1 to Schedule A of the Regulations envisages accounting principles for preparation of financial statements including accounting for investments in standalone financial statement. However, the said Regulations are silent about accounting for Investment in CFS.

Hence, if the financial information of the Investee Bank is excluded from consolidation, whether the same should be accounted as per the principles of AS 13 or as per the applicable Regulations in the CFS.

C. Points considered by the Committee

28. The Committee has analysed the issue raised in the query relating to whether the investment made through and held in PH funds including the investment acquired in 2019 in the Investee Bank (hereinafter referred to as PH investments) qualify to be consolidated under AS 21 or equity accounted as per AS 23 in the consolidated financial statements of the Corporation. The Committee has, therefore, considered only the issue placed before it for opinion and has not examined any other issue(s) that may arise from the facts of the Case. In other words, the Committee has examined, on the basis of mentioned facts, whether the Corporation is to consider the investments made out of PH funds in case the Corporation is liable to prepare CFS as per AS 21 or AS 23 and has not examined IRDAI FS Regulations or IRDA Act. Further, the opinion expressed hereinafter is purely from accounting perspective as per ICAI Accounting Standards and not from the perspective of legal interpretation of IRDA Act, 1999, IRDA Regulations, 2002, LIC Act, 1956, or under any other applicable law or regulation.

The Corporation submitted (in paragraph 3 above) that the bifurcation amongst policyholder of participating and non-participating bifurcation was not maintained for financial reporting purposes by the Corporation in the extant case. Therefore, the Committee presumes that from accounting or financial reporting purposes, these are similar and therefore, the Committee has not examined any distinctive feature existing between these types of policies that may impact the opinion of the Committee (*emphasis supplied*). It is also presumed that in the extant case the querist has referred the issue in the context of non-linked investments. At the outset, the Committee wishes to mention that this opinion is based on the specific facts and circumstances mentioned by the Corporation in the query of the Corporation, same shall not be applied by any other organisation under any circumstances.

29. The Committee notes that Footnote 1 in Accounting Standard (AS) 21, 'Consolidated Financial Statements' and AS 23, 'Accounting for Investments in Associates', issued by the ICAI provides as follows:

AS 21

“It is clarified that AS 21 is mandatory if an enterprise presents consolidated financial statements. In other words, the accounting standard does not mandate an enterprise to present consolidated financial statements but, if the enterprise presents consolidated financial statements for complying with the requirements of any statute or otherwise, it should prepare and present consolidated financial statements in accordance with AS 21.”

AS 23

“It is clarified that AS 23 is mandatory if an enterprise presents consolidated financial statements. In other words, if an enterprise presents consolidated financial statements, it should account for investments in associates in the consolidated financial statements in accordance with AS 23 from the date of its coming into effect, i.e., 1-4-2002 ...”

From the above, the Committee is of the view that the Corporation in the extant case shall apply the requirements of AS 21 and AS 23 only if it presents the consolidated financial statements under the governing statutes or laws applicable to it.

30. In the referred issue, the Committee considers the scope of Accounting Standard (AS) 21, 'Consolidated Financial Statements' as follows:

“1. This Standard should be applied in the preparation and presentation of consolidated financial statements for a group of enterprises under the control of a parent.”

Therefore, in order to qualify for consolidation under AS 21, an investee shall be controlled by the reporting enterprise.

AS 21 further states as follows in paragraphs 5 and 10:

“5.1 Control:

- (a) the ownership, directly or indirectly through subsidiary(ies), of more than one-half of the voting power of an enterprise; or***
- (b) control of the composition of the board of directors in the case of a company or of the composition of the corresponding governing body in case of any other enterprise so as to obtain economic benefits from its activities.”***

“10. The consolidated financial statements are prepared on the basis of financial statements of parent and all enterprises that are controlled by the parent, other than those subsidiaries excluded for the reasons set out in paragraph 11. Control exists when the parent owns, directly or indirectly through subsidiary(ies), more than one-half of the voting power of an enterprise. Control also exists when an enterprise controls the composition of the board of directors (in the case of a company) or of the corresponding governing body (in case of an enterprise not being a company) so as to obtain economic benefits from its activities. An enterprise may control the composition of the governing bodies of entities such as gratuity trust, provident fund trust etc. Since the objective of control over such entities is not to obtain economic benefits from their activities, these are not considered for the purpose of preparation of consolidated financial statements. For the purpose of this Standard, an enterprise is considered to control the composition of:

- (i) the board of directors of a company, if it has the power, without the consent or concurrence of any other person, to appoint or remove all or a majority of directors of that company. An enterprise is deemed to have the power to appoint a director, if any of the following conditions is satisfied:**
 - (a) a person cannot be appointed as director without the exercise in his favour by that enterprise of such a power as aforesaid; or**

- (b) a person's appointment as director follows necessarily from his appointment to a position held by him in that enterprise; or
 - (c) the director is nominated by that enterprise or a subsidiary thereof.
- (ii) the governing body of an enterprise that is not a company, if it has the power, without the consent or the concurrence of any other person, to appoint or remove all or a majority of members of the governing body of that other enterprise. An enterprise is deemed to have the power to appoint a member, if any of the following conditions is satisfied:
- (a) a person cannot be appointed as member of the governing body without the exercise in his favour by that other enterprise of such a power as aforesaid; or
 - (b) a person's appointment as member of the governing body follows necessarily from his appointment to a position held by him in that other enterprise; or
 - (c) the member of the governing body is nominated by that other enterprise.
- ...”

“11. A subsidiary should be excluded from consolidation when:

- (a) control is intended to be temporary because the subsidiary is acquired and held exclusively with a view to its subsequent disposal in the near future; or**
- (b) it operates under severe long-term restrictions which significantly impair its ability to transfer funds to the parent.**

In consolidated financial statements, investments in such subsidiaries should be accounted for in accordance with Accounting Standard (AS) 13, Accounting for Investments. The reasons for not consolidating a subsidiary should be disclosed in the consolidated financial statements.

Explanation:

- (a) *Where an enterprise owns majority of voting power by virtue of ownership of the shares of another enterprise and all the shares are held as ‘stock-in-trade’ and are acquired and held exclusively with a view to their subsequent disposal in the near future, the control by the first mentioned enterprises is considered to be temporary within the meaning of paragraph 11(a).***
- (b) *The period of time, which is considered as near future for the purposes of this Standard primarily depends on the facts and circumstances of each case. However, ordinarily, the meaning of the words ‘near future’ is considered as not more than twelve months from acquisition of relevant investments unless a longer period can be justified on the basis of facts and circumstances of the case. The intention with regard to disposal of the***

relevant investment is considered at the time of acquisition of the investment. Accordingly, if the relevant investment is acquired without an intention to its subsequent disposal in near future, and subsequently, it is decided to dispose off the investments, such an investment is not excluded from consolidation, until the investment is actually disposed off. Conversely, if the relevant investment is acquired with an intention to its subsequent disposal in near future, but, due to some valid reasons, it could not be disposed off within that period, the same will continue to be excluded from consolidation, provided there is no change in the intention.

Further, the Committee notes that in order to qualify for accounting under equity method, the investee shall be significantly influenced by the reporting enterprise. The Committee notes that AS 23, 'Accounting for Investments in Associates' states as follows:

“3.1 An associate is an enterprise in which the investor has significant influence and which is neither a subsidiary nor a joint venture of the investor.

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

3.3 Control:

- (a) The ownership, directly or indirectly through subsidiary(ies), of more than one-half of the voting power of an enterprise; or***
- (b) control of the composition of the board of directors in the case of a company or of the composition of the corresponding governing body in case of any other enterprise so as to obtain economic benefits from its activities.”***

“4. For the purpose of this Standard significant influence does not extend to power to govern the financial and/or operating policies of an enterprise. Significant influence may be gained by share ownership, statute or agreement. As regards share ownership, if an investor holds, directly or indirectly through subsidiary(ies), 20% or more of the voting power of the investee, it is presumed that the investor has significant influence, unless it can be clearly demonstrated that this is not the case. Conversely, if the investor holds, directly or indirectly through subsidiary(ies), less than 20% of the voting power of the investee, it is presumed that the investor does not have significant influence, unless such influence can be clearly demonstrated. A substantial or majority ownership by another investor does not necessarily preclude an investor from having significant influence.

...

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

- (a) Representation on the board of directors or corresponding governing body of the investee;***
- (b) participation in policy making processes;***
- (c) material transactions between the investor and the investee;***

- (d) interchange of managerial personnel; or
- (e) provision of essential technical information.”

Therefore, the Committee notes that under AS 21, control is established either through control of majority of voting power or control over composition of the board of directors of the investee company. Further, under AS 23, an entity is an associate if the investor has significant influence, i.e., power to participate in the financial and/or operating policy decisions of the investee. If an investor, directly or indirectly (through its subsidiaries) holds 20% or more of the voting power of the investee (for example, by way of share ownership), it is presumed that the investor has significant influence, unless it can be demonstrated that this is not the case. In this context, the Committee notes that in the financial year 2019-20, the Corporation acquired 51% stake in ABC Bank Ltd. which was subsequently reduced to 49.24% in the subsequent financial year(s). Further, in this context, the Committee also notes that the querist has specifically stated in the facts of the case that the insurance companies participate and engage with managements of investee companies in capacity of owner of the investments held and not merely as a custodian of PH. There is no distinction in that sense being made as investment forming part of PH or that of SH. However, the Committee notes that facts provided by the querist are silent on control over composition of the board of directors of the investee company as per the requirements of paragraph 10 of AS 21 and other factors determining the existence of significant influence as per the requirements of paragraph 5 of AS 23.

Accordingly, the Committee is of the view that the Corporation appears to have ‘control’ over the ABC Ltd. in financial year 2019-20 by virtue of the ownership of more than one-half of the voting power of the investee enterprise. Further, in subsequent year(s) when shareholding was reduced to 49.24%, by virtue of such shareholding, it can be presumed that the Corporation has significant influence, unless it can be demonstrated that this is not the case. However, in that case also, considering the control over composition of board of directors of the investee company as per the requirements of paragraph 10 of AS 21, it may still be possible that the investee company is controlled by the Corporation. Furthermore, even if it can be demonstrated that inspite of having 49.24% shareholding, the Corporation does not have significant influence over the investee, it may still be possible due to other factors determining the existence of significant influence as per the requirements of paragraph 5 of AS 23 that the Corporation may still have significant influence over the investee in the extant case. Thus, the Committee is of the view that in the extant case, subsequent to reduction in shareholding to 49.24% also, the Corporation shall have control/significant influence over the investee (viz., ABC Bank Ltd.) as per the above-mentioned factors.

31. With regard to exclusion or exception from consolidation under paragraph 11 of AS 21 and related explanations, in cases where the Corporation has control over the investee as per the afore-mentioned discussion and the requirements of AS 21, the Committee is of the view that in the extant case, neither the investment in shares of ABC Bank Ltd. can be considered as stock-in-trade nor held with a view to their disposal in near future as six-years’ term can’t be considered as near future or temporary; and therefore, the control cannot be considered to be temporary. Accordingly, the Committee is of the view that investment in ABC Bank Ltd. cannot be excluded from consolidation under paragraph 11 of AS 21.

32. With regard to the querist's contention in relation to 'control' over policyholders' funds, the Committee notes from the Facts of the Case that the investments by the Corporation from PH funds are generally made with a view to generate adequate periodic returns/gains therefrom so as to protect the interest of PHs and to provide required liquidity for meeting claims, surrenders and other obligations on the life insurance policies written. These investments are under regulatory ring-fenced structure, being subject to several regulatory limits/conditions and are required to be maintained separately from SH Funds under the provisions of applicable law and regulations. In the balance sheet of the Corporation, PH funds are shown as liabilities.

Further, it has been specifically stated by the querist in the Facts of the Case, that for the investment made either from PH fund or SH fund, the rights, and obligations w.r.t. that investment is to be always borne by the insurance company (i.e., ultimately by the SH). For investments made from PH funds, for the obligations, if at all, at segment level shall be borne by SHs. For instance, if a deficit is created due to diminution in the fair value change of investment made in debenture instrument from PH fund impacting the solvency ratio, this deficit is required to be made good by the SH.

The Committee also analyses the nature of insurance business, where, when the Corporation received funds from policyholders on account of insurance policy written, it accepts a liability towards the policyholders to the extent of sum assured as per the terms of the insurance policy. If any contingent situation happens as per the terms and conditions of the policy, then the commitment towards the sum assured has to be honored/met whether the PH funds are sufficient or not. In other words, if PH funds are not sufficient, as per the terms of the policy, the same shall be met by the Corporation out of the SH funds.

Considering the above submissions made by the querist and considering the nature of insurance business, the Committee is of the view that in the extant case, the funds received from the policyholders create an obligation for the Corporation to provide adequate returns out of the investments made out of such funds as well as to provide required liquidity for meeting claims, surrenders and other obligations on the life insurance policies written and thus, results into liabilities in respect of obligations undertaken. In order to fulfill these obligations, the Corporation makes investments on its own account, which gives rise to a corresponding asset in terms of investment made out of such funds as the Corporation seems to have decision making rights in the investee companies.

The Corporation is managing the PH investments and a portion of the surplus of the PH investments is credited to SH funds. Thus, the Corporation would benefit as a consequence of creating surplus for the policyholders. Therefore, the Corporation has economic benefits arising from the PH investments.

33. Based on the above, it seems that, overall, the investments made out of PH funds would result in control/significant influence by the Corporation on its own account for the purpose of AS 21/AS 23 and therefore, the corporation should consolidate or follow equity accounting as per the relevant requirements of AS 21 and AS 23 respectively.

D. Opinion

34. On the basis of above, the Committee is of the following opinion on the issues raised in paragraph 27 above:

- (i) The investment made through and held in PH funds is an investment made by the Corporation on its account to meet its obligation/liability created as per the terms of the insurance policy on account of PH funds received and the same shall be consolidated/equity accounted in the consolidated financial statements of the Corporation, as discussed in paragraphs 30 to 33 above. The Corporation in the extant case shall apply the requirements of AS 21 and AS 23 only if it presents the consolidated financial statements under the governing statutes or laws applicable to it.
- (ii) In the given facts and circumstances of the matter, the control held by the Corporation in the extant case cannot be excluded from consolidation under paragraph 11(a) of AS 21.
- (iii) Since the financial information of the Investee Bank is not to be excluded from the consolidation, answer to this question does not arise.
