Query No. 6

Subject: ***Accounting treatment of similar leasehold assets held by parent and subsidiary company with different functional currencies and consolidation thereof under Ind AS framework.***[1]

A. Facts of the Case

1. A public limited company (Child Ltd. or 'the Company'), which is a wholly owned subsidiary of a listed public sector undertaking company (Parent Ltd.), is in the business of exploration and production of oil and gas and other hydrocarbon related activities outside India. Child Ltd. operates overseas projects directly and/or through subsidiaries, by participation in various joint arrangements and investment in associates.

2. Child Ltd. has adopted Indian Accounting Standards (Ind AS) w.e.f. 1st April 2016 (Transition Date: 1st April 2015). The functional currency of Child Ltd. is assessed as US Dollar (USD) in accordance with the provisions of Indian Accounting Standards (Ind AS). It presents its financial statements in presentation currency which is Indian Rupee (INR).

3. Parent Ltd., which is in the business of exploration and production of oil and gas and other hydrocarbon related activities in India adopted Indian Accounting Standards (Ind AS) w.e.f. 1st April 2016 (Transition Date: 1st April 2015). It prepares and presents its financial statements in its functional currency INR.

4. As stated in paragraph 2 above, functional currency of Child Ltd. has been determined as US Dollar (USD) based on the evaluation of the primary economic environment in which the Company operates and primarily generates and expends cash. Child Ltd. is required to present its financial statements in Indian Rupees (INR) as per Schedule III to the Companies Act, 2013. The USD functional currency financial statements of Child Ltd. are then translated into INR in line with provisions of Ind AS 21, 'The Effects of Changes in Foreign Exchange Rates' for presentation purposes. It applies the following principles for translating its financial statements from functional currency USD to presentation currency INR:

- Assets and liabilities (excluding equity share capital and other reserves) for each balance sheet presented are translated at the closing rate at the date of that balance sheet;
- Equity share capital is translated at exchange rates at the dates of transactions. Capital reserve is translated at exchange rate at the dates of transactions. Other reserves have been translated using average exchange rates of the period to which they relate;
- Income and expenses have been translated at exchange rates at the dates of transactions except for certain items for which average rate for the period is used;
- All exchange differences resulting from translation of financial statements from functional currency to presentation currency have been recognised in other comprehensive income as 'Exchange differences in translating the financial statements of foreign operations'.

5. Child Ltd. and Parent Ltd. acquired adjacent pieces of land from State Development Authority on perpetual lease in December 2003 which were capitalised as leasehold asset

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[1] Opinion finalised by the Committee on 19.4.2023 and 20.4.2023.

under the head ‘Other Property, Plant and Equipment’ at the time of Ind AS transition in the respective separate financial statements of both the companies. The upfront premium and yearly lease rentals for the respective pieces of land acquired by both the companies are same, the acquisition value of leasehold land was same, i.e., INR 200 crore for both the companies at the time of acquisition. The departure, however, lies in the fact that for Parent Ltd., the transaction was in its functional currency INR, but for Child Ltd., the transaction was a foreign currency transaction since for Child Ltd., INR is a foreign currency.

6. The querist has stated that following the provisions of Ind AS 101, ‘First-time Adoption of Indian Accounting Standards’ and the erstwhile Ind AS 17, ‘Leases’, Child Ltd. classified lease in respect of its piece of the said land as a finance lease at the time of Ind AS transition and capitalised the upfront one-time lease premium paid along with stamp duty and yearly lease rent payable at a value of Rs. 200 crore (equivalent to USD 46 million as at transaction date) as leasehold land in its ‘Property, Plant and Equipment (PPE)’. Upon implementation of new Ind AS 116, ‘Leases’, the said asset i.e. leasehold land was rechristened as ‘Right of Use (ROU) Asset-leasehold land’ at the same value USD 46 million. In accordance with the provisions of Ind AS 116 and Ind AS 21, the Company recognised and subsequently carries the leasehold land at historical cost (applying cost model) as determined in its functional currency USD. Thus, the Company initially recognised the leasehold land at USD 46 million as PPE and measures the said asset on subsequent reporting dates (firstly as PPE and subsequently as ROU assets) at the same historical value of USD 46 million. Upon translating the functional currency USD financials to presentation currency INR financials on balance sheet date, the value of such leasehold land is translated to INR at closing exchange rate. Accordingly, the value of leasehold land as appearing in the financial statements of the Company in presentation currency INR as at 31st March 2022 is INR 350 crore.

7. On the other hand, since the functional currency of Parent Ltd. is INR, it had recognised its part of leasehold land at historical cost in INR and accordingly carries the said assets at INR 200 crore.

8. Thus, in respect of similar items of asset, Child Ltd. and Parent Ltd. carry their respective leasehold lands at different carrying values despite of same acquisition costs in transaction currency. This difference is due to determination of historical costs of said assets in different functional currencies. Though both the companies have acquired the said assets in INR but in case of Parent Ltd., since the functional and presentation currency is INR the leasehold land was initially recognised at historical value INR 200 crore and same value continues to be reported in the financial statements. However, in case of Child Ltd., since the functional currency is USD, the historical value was determined by translating the INR value incurred on the acquisition date into functional USD by applying exchange rate as at the date of transaction. The leasehold land is continued to be measured by Child Ltd. at the said historical value fixed in USD, viz., USD 46 million. For reporting purposes, in order to translate the financial statements from functional currency (USD) to presentation currency INR, the value of the assets is reconverted applying the closing exchange rate as per Ind AS 21 and therefore, at each balance sheet date, the carrying value of leasehold land is converted from the said historical value of USD 46 million into presentation currency INR by applying closing exchange rate. Due to appreciation in the USD exchange rate since acquisition time, the carrying value of the leasehold land in presentation currency INR has increased significantly (from INR 200 crore as at transaction date to INR 350 crore as at March 31, 2022). The resulting exchange difference has been recognised in ‘Foreign Currency Translation Reserve (FCTR)’ through Other Comprehensive Income (OCI) of respective years. On the other hand, for Parent Ltd., the value of its part of leasehold land is maintained,

i.e., INR 200 crore. While preparing the consolidated financial statements for the Group for financial year (F.Y.) 2021-22, Parent Ltd. has consolidated the carrying value of leasehold land of the Company valued at INR 350 crore in presentation currency INR with its own part of leasehold land continued to be valued at INR 200 crore. Therefore, in the consolidated financial statements of the Group, two similar assets within the Group, in the form of two similar adjacent pieces of land, acquired at the same time and at same value by the Group (even though by different components of the Group viz. Parent Company and the Company) are being measured and carried at different values in terms of presentation currency INR.

Issue in question:

9. During the course of supplementary audit for the financial year ended 31st March 2022 of Child Ltd., Comptroller and Auditor General of India (C&AG) auditors raised an observation that this land was capitalised by Child Ltd. at an amount of Rs. 200 crore being the actual cost whereas the same has gradually been increased to Rs. 350 crore by including the effect of exchanges differences. Thus, it includes an appreciation of Rs. 150 crore (around 73 per cent increase) in the cost of land which is a material amount and therefore, should have been disclosed appropriately by way of foot note / reference to the above note. Further, the cumulative effect of exchange differences on account of translation from functional currency to presentation currency should have been clearly segregated / presented apart from actual cost of land considering the money measurement concept. Audit also observed that an identical piece of adjacent land acquired by Parent Ltd. is being shown by Parent Ltd. at original value. Thus, in order to bring clarity and for better presentation of the facts and accounting treatment applied by the Company, the disclosures need to be modified appropriately. Further, other disclosures in respect of similar transactions also need to be reviewed and modified suitably.

10. According to the auditors, the financial statements of Child Ltd. do not inform the stakeholders about historical cost in presentation currency in view of different functional and presentation currency adopted by the Company.

11. Subsequently during follow up meeting, the auditors pointed out that even though both the companies, Child Ltd. as well as Parent Ltd. have been doing correct accounting treatment in respect of their leasehold land individually in their respective financial statements in compliance with the requirements of relevant Ind AS provisions, but in the consolidated financial statements of Parent Ltd., the correct picture is not presented as two same kind of assets, acquired by the Group (through Parent Ltd. and Child Ltd. respectively) at the same time and at same original acquisition value are now being presented at different carrying value in INR and therefore, in the consolidated financial statements of Parent Ltd., appropriate adjustments should be made in order to reflect the value of leasehold land of Child Ltd. at its original INR value as at acquisition date instead of INR value translated in INR by applying closing exchange rate from historical cost determined in functional currency USD.

Company's perspective:

12. The recognition, measurement and presentation of the leasehold land has been done by the Company and Parent Company in their respective financial statements in accordance with applicable Ind AS provisions. Moreover, the consolidation of value of leasehold land of Child Ltd. in the consolidated financial statements of Parent Ltd. has also been done in accordance with the provisions of Ind AS 110, 'Consolidated Financial Statements'.

Financial Statements of Child Ltd.

13. The querist has stated that Child Ltd. had obtained the land on perpetual lease in the year 2004 by paying an upfront premium of Rs. 127 crore. Along with incidental transaction costs of Rs. 40 crore, the total lease was capitalised at Rs. 167 crore. The said transaction was incurred prior to implementation of Ind AS, and in accordance with previous GAAP, the upfront premium paid along with incidental costs was capitalised as leasehold land and the yearly rental was charged off to the Statement of Profit and Loss considering the same as operating lease. As on the date of transition to Ind AS, the Company classified the leasehold land as finance lease and accordingly applied paragraph D9AA of Ind AS 101 (First-time Adoption of Indian Accounting Standards) which states that "[2]When a lease includes both land and building elements, a first time adopter lessor may assess the classification of each element as finance or an operating lease at the date of transition to Ind ASs on the basis of the facts and circumstances existing as at that date. *If there is any land lease newly classified as finance lease, then the first time adopter may recognise assets and liability at fair value on that date; and any difference between those fair values is recognised in retained earnings"*. (Emphasis supplied by the querist.) Accordingly, upon transition, the leasehold land was recognised as an asset under 'Other Property, Plant and Equipment' at fair value thereof which was calculated taking the overall consideration for lease into account which included upfront premium and incidental costs as well as present value of annual lease rentals till perpetuity. Subsequent to the introduction of new Ind AS on Leases viz., Ind AS 116, the Company had applied cumulative catch up or modified retrospective method of transition in accordance with paragraphs C3, C4 and C5(b) of Ind AS 116 and accordingly recognised the Right of Use asset in respect of the leasehold land at the same carrying value as that of leasehold land classified as asset under finance lease under Ind AS 17 prior to introduction of Ind AS 116. The recognition and subsequent measurement of right-of-use asset at each reporting date for the leasehold land is in accordance with paragraphs 23 to 33 of Ind AS 116 which state that at the commencement date, a lessee shall measure the right-of-use asset at cost and the cost of the right-of-use asset shall, inter alia, comprise the amount of initial measurement of the lease liability (including fixed and variable lease payments) and any lease payments made at or before the commencement date. It is also stated that after the commencement date, a lessee shall measure the right-of-use asset applying the cost model unless it applies the measurement model. Thus, the above-mentioned provisions state the quantum at which leasehold land obtained by Child Ltd. is required to be initially recognised and subsequently carried in its financial statements.

14. As regards the currency in which the said leasehold land is required to be initially recognised and subsequently carried in the financial statements of Child Ltd., it is imperative to refer the provisions of Ind AS 21. Since the functional currency of the Company is USD which is different from its presentation currency INR, in the instant case, provisions of Ind AS 21 relating to functional currency shall also apply in addition to the provisions of Ind AS 116 as stated above. The Standard defines 'Foreign Currency' as the currency other than the functional currency of the entity. It further defines 'Presentation Currency' as the currency in which the financial statements are presented. Thus, currency INR is foreign currency as well as presentation currency for the Company. Paragraph 20 of the Ind AS 21 states as follows:

> "A *foreign currency transaction* is a transaction that is denominated or requires settlement in a foreign currency, including transactions arising when an entity:

[2] Substituted vide Notification No. G.S.R. 273(E) dated 30th March, 2019.

(a) …

(b) …

(c) otherwise *acquires or disposes of assets*, or incurs or settles liabilities, denominated in a foreign currency." (Emphasis supplied by the querist.)

Thus, the acquisition of leasehold land in INR currency is a foreign currency transaction as it is a transaction wherein the entity has acquired the assets in a currency (INR) which is different from its functional currency USD.

Further, paragraph 21 of Ind AS 21 states that **"A *foreign currency transaction shall be recorded, on initial recognition in the functional currency*, by applying to the foreign currency amount the *spot exchange rate* between the functional currency and the foreign currency *at the date of the transaction.*"** (Emphasis supplied by the querist.)

Thus, where the provisions of Ind AS 116 mentioned above provide the quantum, i.e., the cost at which the leasehold land shall be recognised, provisions of Ind AS 21 as stated above provide currency and manner in which such leasehold land shall be recognised. Therefore, a conjunctive reading of above provision suggests that the item of leasehold asset shall be recognised at cost but the cost that has been incurred in foreign currency shall be converted into functional currency by applying the spot exchange rate between the functional currency and the foreign currency at the date of the transaction and the assets so acquired in a foreign currency transaction shall be initially recognised in functional currency so computed.

Regarding subsequent reporting, paragraph 23 of Ind AS 21 states, **"At the end of each reporting period:**

(a) …

(b) *non-monetary items that are measured in terms of historical cost in a foreign currency* shall be translated using the exchange rate at the *date of the transaction*; and

(c) ..." (Emphasis supplied by the querist.)

The overall effect of the above provisions is that the leasehold asset is initially recognised at cost and such cost is recorded in terms of functional currency thereby ensuring compliance with the requirements of both Ind AS 116 and Ind AS 21. Subsequent reporting of the asset in functional currency is also done using the historical exchange rate as per paragraph 23 of Ind AS 21. Furthermore, as regards translation from foreign currency into functional currency, paragraph 34 of Ind AS 21 states, inter alia, that "non-monetary items that are measured on a historical cost basis are translated using the exchange rate at the date of the transaction that resulted in their recognition."

Therefore, the land, in the given case, has been initially recorded and subsequently measured at cost as per Ind AS 116 and the said historical cost has been recorded in functional currency i.e. USD as per the requirements of Ind AS 21 using the historical exchange rate at the date of transaction.

15. As regards translating into presentation currency, paragraph 39 of Ind AS 21 states that **"The results and financial position of an entity whose functional currency is not the**

currency of a hyperinflationary economy shall be translated into a different presentation currency using the following procedures:

(a) ***assets and liabilities* for each balance sheet presented (ie including comparatives) shall be translated *at the closing rate at the date of that balance sheet;***

(b) **income and expenses for each statement of profit and loss presented (ie including comparatives) shall be translated at exchange rates at the dates of the transactions; and**

(c) **all resulting exchange differences shall be recognised in other comprehensive income.** (Emphasis supplied by the querist.)

Thus, for translating the Company's functional currency financial statements to presentation currency (i.e. INR), the Company uses the translation procedure as listed out in Ind AS 21. The USD value of such land has been fixed at the date of capitalisation of such land. As the Company Child Ltd. presents its financial statements in INR, USD 46 million is converted at the reporting date rate to INR, with the difference in the INR values being recognised as foreign currency translation reserve (FCTR). Currently, the Company is presenting such land at a value of Rs. 350 crore (as on 31.03.2022) which represents USD value multiplied by the reporting date USD vs INR exchange rate. This procedure, as per the querist, is as per the requirements of Ind AS 21.

16. In the light of above provisions, according to the querist, the current practice of the Company reporting the land at historical cost in functional currency and translating the same in presentation currency using the closing exchange rate is in compliance with the applicable provisions of applicable Ind AS.

17. Moreover, in order to assist the users of financial statements of the Company to understand the accounting for such assets, following explanatory note has been given in the financial statements of the Company:

> The functional currency of the Company is US Dollar. Hence, all items of Property, Plant & Equipment acquired by the Company are recognised at historical cost at the rate on the date of acquisition of such assets, including assets acquired originally in Indian Rupees located in India. For the purpose of preparing these financial statements, the US Dollar values of these assets are translated from US Dollar to INR (presentation currency) at the reporting date exchange rate.

Separate Financial Statements of Parent Ltd.:

18. In the separate financial statements of Parent Ltd., the value of its own leasehold land has been initially recognised at INR 200 crore and the said asset continues to be measured at same historical value determined in INR in accordance with the Ind AS provisions as described in paragraph 13 above. The said accounting treatment is in accordance with Ind AS 116.

Consolidated Financial Statements of Parent Ltd.

19. Parent Ltd. prepares its consolidated financial statements in INR currency. Therefore, Child Ltd. has to submit its financial statements to Parent Ltd. as translated in presentation INR currency. As required by paragraph B86 of Ind AS 110, 'Consolidated Financial Statements', while consolidating, Parent Ltd., inter alia, combines like items of its own assets with those of subsidiaries including Child Ltd. Thus, the value of leasehold land as appearing in Parent Ltd. at INR 200 crore is combined with the value of leasehold land of Child Ltd. converted in presentation currency INR at INR 350 crore. Provisions of Ind AS 110 do not require any adjustments in respect of such translated value of assets in respect of any subsidiaries. The mandate of consolidation procedures as provided in paragraph B86 of Ind AS 110 is to combine the values of like items of assets, liabilities etc. of parent with those of its subsidiaries and to eliminate intragroup transactions and balances. Any other adjustments for presenting the value of any assets at their original acquisition value in foreign currency to remove the effect of exchange rate difference arising due to translation of functional currency financial statements into presentation currency is not required by the Ind AS. Thus, as per the querist, the Parent Ltd. has correctly consolidated the value of leasehold land of Child Ltd. in its consolidated financial statements.

20. In the light of foregoing, Child Ltd. is of the view that it has done correct recognition and measurement of its leasehold land in accordance with the provisions of Ind AS in its financial statements. Further, Parent Ltd. has correctly done consolidation of such leasehold land in its consolidated financial statements and no adjustment is required in the consolidated financials of Parent Ltd. in this regard.

B. Query

21. In view of the above facts, the opinion of the Expert Advisory Committee of the Institute of Chartered Accountants of India is solicited on the following:

Whether-

(i) in case of non-monetary items, where the transaction currency (INR) is same as presentation currency (INR) but is different from functional currency (USD), translation of such non-monetary items first from transaction currency (INR) to functional currency (USD) at transaction date and then from functional currency (USD) to presentation currency (INR) again at reporting date is required as per Ind AS provisions.

(ii) in the light of provisions of Ind AS 116 and Ind AS 21, the company Child Ltd. has correctly accounted for its part of leasehold land in its financial statements and has provided adequate disclosure in respect of the same.

(iii) any further disclosure is required by relevant Ind AS in this regard.

(iv) any adjustments are required to be made in the consolidated financial statements of Parent Ltd. for presenting the value of leasehold land of Child Ltd. at its original acquisition value to remove the effect of exchange rate difference arising due to translation of functional currency (USD) financial statements into presentation currency (INR).

C. Points considered by the Committee

22. The Committee notes that the basic issue raised in the query relates to translation of leasehold land held by Child Ltd. (having a different functional currency from the presentation currency) for the purpose of reporting in its separate financial statements and whether any adjustments are required to be made to the value of leasehold land of Child Ltd. for presenting in the consolidated financial statements of Parent Ltd. The Committee has therefore, examined only these issues and has not examined any other issue that may arise from the Facts of the case, such as, lease accounting as per the requirements of Ind AS 116, 'Leases', determination of functional currency of Child Ltd. and Parent Ltd., restatement or translation of other items for the purpose of reporting in the financial statements, accounting for exchange differences, accounting for incidental transaction costs, transition from the erstwhile standards on leases to Ind AS 116, accounting at the time of transition to Ind AS, recognition and measurement of Right of use asset, whether the parent company controls the subsidiary as per the principles of Ind AS 110, Consolidated Financial Statements, impairment of RoU asset in the financial statements of Parent Ltd. and Child Ltd., etc. The Committee also notes that the querist has not raised the query with regard to lease liability corresponding to leasehold/RoU land in the extant case and therefore, the Committee has not examined the same. Further, the Committee wishes to point out that the Indian Accounting Standards referred to in the Opinion are the Standards notified under the Companies (Indian Accounting Standards) Rules, 2015, as revised or amended from time to time.

23. The Committee notes the following requirements of Ind AS 21, 'The Effects of Changes in Foreign Exchange Rates':

"3 This Standard shall be applied:

> **(a) in accounting for transactions and balances in foreign currencies, except for those derivative transactions and balances that are within the scope of Ind AS 109, *Financial Instruments*;**
>
> **(b) in translating the results and financial position of foreign operations that are included in the financial statements of the entity by consolidation or the equity method; and**
>
> **(c) in translating an entity's results and financial position into a presentation currency."**

"6 This Standard applies to the presentation of an entity's financial statements in a foreign currency and sets out requirements for the resulting financial statements to be described as complying with Indian Accounting Standards (Ind ASs). For translations of financial information into a foreign currency that do not meet these requirements, this Standard specifies information to be disclosed."

"Foreign currency **is a currency other than the functional currency of the entity.**

Foreign operation **is an entity that is a subsidiary, associate, joint arrangement or branch of a reporting entity, the activities of which are based or conducted in a country or currency other than those of the reporting entity.**

Functional currency **is the currency of the primary economic environment in which the entity operates.**

A *group* is a parent and all its subsidiaries.

***Monetary items* are units of currency held and assets and liabilities to be received or paid in a fixed or determinable number of units of currency."**

"Monetary items

16 The essential feature of a monetary item is a right to receive (or an obligation to deliver) a fixed or determinable number of units of currency. Examples include: pensions and other employee benefits to be paid in cash; provisions that are to be settled in cash; **lease liabilities**; and cash dividends that are recognised as a liability. Similarly, a contract to receive (or deliver) a variable number of the entity's own equity instruments or a variable amount of assets in which the fair value to be received (or delivered) equals a fixed or determinable number of units of currency is a monetary item. Conversely, the essential feature of a non-monetary item is the absence of a right to receive (or an obligation to deliver) a fixed or determinable number of units of currency. Examples include: amounts prepaid for goods and services; goodwill; intangible assets; inventories; property, plant and equipment; **right-of-use assets** and provisions that are to be settled by the delivery of a non-monetary asset. (Emphasis supplied by the Committee.)

Summary of the approach required by this Standard

17 In preparing financial statements, each entity—whether a stand-alone entity, an entity with foreign operations (such as a parent) or a foreign operation (such as a subsidiary or branch)—determines its functional currency in accordance with paragraphs 9–14. The entity translates foreign currency items into its functional currency and reports the effects of such translation in accordance with paragraphs 20–37 and 50.

18 Many reporting entities comprise a number of individual entities (eg a group is made up of a parent and one or more subsidiaries). Various types of entities, whether members of a group or otherwise, may have investments in associates or joint arrangements. They may also have branches. It is necessary for the results and financial position of each individual entity included in the reporting entity to be translated into the currency in which the reporting entity presents its financial statements. This Standard permits the presentation currency of a reporting entity to be any currency (or currencies). The results and financial position of any individual entity within the reporting entity whose functional currency differs from the presentation currency are translated in accordance with paragraphs 38–50.

19 This Standard also permits a stand-alone entity preparing financial statements or an entity preparing separate financial statements in accordance with Ind AS 27, *Separate Financial Statements*, to present its financial statements in any currency (or currencies). If the entity's presentation currency differs from its functional currency, its results and financial position are also translated into the presentation currency in accordance with paragraphs 38–50.

Reporting foreign currency transactions in the functional currency

Initial recognition

20 A foreign currency transaction is a transaction that is denominated or requires settlement in a foreign currency, including transactions arising when an entity:

(a) buys or sells goods or services whose price is denominated in a foreign currency;

(b) borrows or lends funds when the amounts payable or receivable are denominated in a foreign currency; or

(c) otherwise acquires or disposes of assets, or incurs or settles liabilities, denominated in a foreign currency.

21 A foreign currency transaction shall be recorded, on initial recognition in the functional currency, by applying to the foreign currency amount the spot exchange rate between the functional currency and the foreign currency at the date of the transaction.”

“Reporting at the ends of subsequent reporting periods

23 At the end of each reporting period:

(a) foreign currency monetary items shall be translated using the closing rate;

(b) non-monetary items that are measured in terms of historical cost in a foreign currency shall be translated using the exchange rate at the date of the transaction; and

(c) non-monetary items that are measured at fair value in a foreign currency shall be translated using the exchange rates at the date when the fair value was measured.”

“34 When an entity keeps its books and records in a currency other than its functional currency, at the time the entity prepares its financial statements all amounts are translated into the functional currency in accordance with paragraphs 20–26. This produces the same amounts in the functional currency as would have occurred had the items been recorded initially in the functional currency. For example, monetary items are translated into the functional currency using the closing rate, and non-monetary items that are measured on a historical cost basis are translated using the exchange rate at the date of the transaction that resulted in their recognition.”

The Committee notes from the above that the Standard requires that while preparing financial statements, each entity shall translate foreign currency items, i.e., items that are denominated in a currency other than its functional currency, into its functional currency and report the effects of such translation in accordance with paragraphs 20–37 and 50. Further, it states that the results and financial position of any individual entity within the reporting entity whose functional currency differs from the presentation currency are translated in accordance with paragraphs 38–50.

The Committee notes from the Facts of the Case that for Child Ltd., functional currency is US

Dollars (USD) and therefore, any other currency including Indian Rupee (INR) is a foreign currency. Since, the RoU asset, acquired by Child Ltd. is denominated in foreign currency, this transaction is a foreign currency transaction as per paragraph 20(c) of Ind AS 21. Therefore, on initial recognition, Child Ltd. should translate such foreign currency item into its functional currency by applying the spot exchange rate between the functional currency and the foreign currency at the date of the transaction. Thus, the transaction should be recognised at the exchange rate on the date of transaction. With regard to subsequent measurement, the Standard requires that at the end of reporting date, non-monetary items that are measured in terms of historical cost in a foreign currency shall be translated using the exchange rate at the date of the transaction. Since the RoU land is a non-monetary asset as per paragraph 16 of Ind AS 21 in the extant case, it will be translated using the exchange rate at the date of the transaction for the purpose of preparing the financial statements in functional currency.

24. The Committee further notes that the Standard also requires that when an entity presents its financial statements in a currency other than its functional currency i.e. when the presentation currency and functional currency are different, it has to translate its results into presentation currency considering the following requirements of Ind AS 21:

> **"Translation to the presentation currency**
>
> 38 An entity may present its financial statements in any currency (or currencies). If the presentation currency differs from the entity's functional currency, it translates its results and financial position into the presentation currency. For example, when a group contains individual entities with different functional currencies, the results and financial position of each entity are expressed in a common currency so that consolidated financial statements may be presented.
>
> **39 The results and financial position of an entity whose functional currency is not the currency of a hyperinflationary economy shall be translated into a different presentation currency using the following procedures:**
>
> **(a) assets and liabilities for each balance sheet presented (ie including comparatives) shall be translated at the closing rate at the date of that balance sheet;**
>
> **(b) income and expenses for each statement of profit and loss presented (ie including comparatives) shall be translated at exchange rates at the dates of the transactions; and**
>
> **(c) all resulting exchange differences shall be recognised in other comprehensive income."**

From the above, the Committee notes that when the presentation currency is different from functional currency, the assets and liabilities for each balance sheet date are translated using the closing rate at the date of balance sheet, irrespective of whether such items are monetary or non-monetary. Thus, in the extant case, since Child Ltd. is presenting its financial statements in INR, it has to translate the right-of-use land at the closing exchange rate at the balance sheet date for the purpose of presenting its financial statements in INR, viz., the presentation currency. Further, the Company has to provide disclosures as per paragraphs

53 and 55 of Ind AS 21. The Committee is of the view that the above translation shall result into the exchange difference from the date of transaction till the reporting date being recognised in other comprehensive income over the years. It represents foreign exchange fluctuation in the functional currency vis-a-vis the reporting currency, which is not a real gain or loss incurred by the entity. Since the carrying value of asset has increased or decreased in terms of the presentation currency when compared to the functional currency, the same is reflected in the financial statements.

25. With regard to presentation in the consolidated financial statements of Parent Ltd., the Committee notes the following requirements of Ind AS 21 and Ind AS 110, Consolidated Financial Statements:

Ind AS 21

"Translation of a foreign operation

44 Paragraphs 45–47, in addition to paragraphs 38–43, apply when the results and financial position of a foreign operation are translated into a presentation currency so that the foreign operation can be included in the financial statements of the reporting entity by consolidation or the equity method.

45 The incorporation of the results and financial position of a foreign operation with those of the reporting entity follows normal consolidation procedures, such as the elimination of intragroup balances and intragroup transactions of a subsidiary (see Ind AS 110, *Consolidated Financial Statements*). However, an intragroup monetary asset (or liability), whether short-term or long-term, cannot be eliminated against the corresponding intragroup liability (or asset) without showing the results of currency fluctuations in the consolidated financial statements. This is because the monetary item represents a commitment to convert one currency into another and exposes the reporting entity to a gain or loss through currency fluctuations. Accordingly, in the consolidated financial statements of the reporting entity, such an exchange difference is recognised in profit or loss or, if it arises from the circumstances described in paragraph 32, it is recognised in other comprehensive income and accumulated in a separate component of equity until the disposal of the foreign operation."

Ind AS 110

"19 A parent shall prepare consolidated financial statements using uniform accounting policies for like transactions and other events in similar circumstances."

"B86 Consolidated financial statements:

(a) combine like items of assets, liabilities, equity, income, expenses and cash flows of the parent with those of its subsidiaries.

(b) offset (eliminate) the carrying amount of the parent's investment in each subsidiary and the parent's portion of equity of each subsidiary (Ind AS 103 explains how to account for any related goodwill).

(c) eliminate in full intragroup assets and liabilities, equity, income, expenses and cash flows relating to transactions between entities of the group (profits or losses resulting from intragroup transactions that are recognised in assets, such as inventory and fixed assets, are eliminated in full). Intragroup losses may indicate an impairment that requires recognition in the consolidated financial statements. Ind AS12, *Income Taxes*, applies to temporary differences that arise from the elimination of profits and losses resulting from intragroup transactions."

The Committee notes that paragraph 18 of Ind AS 21 states that it is necessary for the results and financial position of each individual entity included in the reporting entity to be translated into the currency in which the reporting entity presents its financial statements. Similarly, paragraph 44 states that to include the foreign operation in the financial statements of the reporting entity by consolidation or the equity method, the results and financial position of a foreign operation are translated into the presentation currency of the reporting entity. For this purpose, the results and financial position of the foreign operation are translated in accordance with paragraphs 38–50. Thus, in the extant case, to incorporate the results and financial position of Child Ltd. with those of the reporting entity (Parent Ltd.), the Parent entity has to translate the results and financial position of Child Ltd. into its presentation currency in accordance with paragraphs 38–50 of Ind AS 21. Therefore, as per the requirements of paragraph 39 of Ind AS 21, the assets and liabilities of Child Ltd. for each balance sheet presented (ie including comparatives) shall be translated at the closing rate at the date of that balance sheet. Thus, the RoU land of Child Ltd. shall appear in the consolidated financial statements of Parent Ltd. after translating its value in functional currency (viz., USD) into presentation currency of Parent Ltd. (viz., INR) using the exchange rates at the date of the balance sheet. The Committee notes that Ind AS 110 does not give any exception to this requirement and requires to follow normal consolidation procedures to combine like items of assets, liabilities, equity, income, expenses and cash flows of the parent with those of its subsidiaries. Thus, the above translation and incorporation of assets of Child Ltd. shall result into the exchange difference from the date of transaction till the reporting or balance sheet date to be recognised even in the consolidated financial statements and the value of RoU of land of Child Ltd. shall appear at its revised translated amount using the exchange rate at the balance sheet date of the Parent Ltd.

26. With regard to the presentation and disclosure of the RoU land in the financial statements of Child Ltd. and Parent Ltd., the Committee notes paragraph 53(h) of Ind AS 116 which states as follows:

"Disclosure

…

53 A lessee shall disclose the following amounts for the reporting period:

…

(h) additions to right-of-use assets;

…"

From the above, the Committee is of the view that the additions to right-of-use assets for the reporting period, should also include the net exchange differences arising on the translation of the financial statements from the functional currency into a different presentation currency, including translation of the foreign operation into the presentation currency of the reporting entity.

D. Opinion

27. On the basis of the above, the Committee is of the following opinion on the issues raised in paragraph 21 above:

(i) and (ii) The translation of leasehold or RoU assets held by Child Ltd. (having a different functional currency from the presentation and transaction currency), first from transaction currency (INR) to functional currency (USD) at transaction date and then from functional currency (USD) to presentation currency (INR) at the reporting date in its separate financial statements is in accordance with the requirements of Ind AS 21. Further, the Company has to provide disclosures as per paragraphs 53 and 55 of Ind AS 21 and appropriate disclosures as per Ind AS 116, as discussed in paragraph 26 above. As mentioned in paragraph 22 above, the issue has not been examined from the perspective of Ind AS 116.

(iii) This is a generic question that cannot be answered by the Committee.

(iv) The RoU land of Child Ltd. shall appear in the consolidated financial statements of Parent Ltd. after translating its value in functional currency (viz., USD) into presentation currency of Parent Ltd. (viz., INR) using the exchange rates at the date of the balance sheet. The Committee notes that Ind AS 110 does not give any exception to this requirement. Therefore, presentation of right-of-use asset of Child Ltd. at the revised translated amount using the exchange rate at the balance sheet date of Parent Ltd., in the consolidated financial statements of Parent Ltd. is in accordance with the requirements of Ind AS 110. However, appropriate disclosures as per Ind AS 116, as discussed in paragraph 26 above, should also be made in the financial statements.

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